

# Restructuring & Insolvency

*Contributing editor*  
**Bruce Leonard**



2017

GETTING THE  
DEAL THROUGH

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DEAL THROUGH 

# Restructuring & Insolvency 2017

*Contributing editor*

**Bruce Leonard**

**The International Insolvency Institute**

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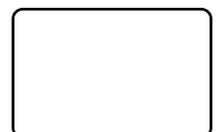


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## CONTENTS

<b>Global overview</b>	<b>7</b>	<b>Cyprus</b>	<b>129</b>
Richard Tett Freshfields Bruckhaus Deringer		Lia Iordanou Theodoulou, Angeliki Epaminonda and Stylios Trillides Patrikios Pavlou & Associates LLC	
<b>Australia</b>	<b>9</b>	<b>Dominican Republic</b>	<b>138</b>
Dominic Emmett and Sabrina Ng Gilbert + Tobin		Mary Fernández, Jaime Senior and Melba Alcántara Headrick	
<b>Austria</b>	<b>22</b>	<b>England &amp; Wales</b>	<b>149</b>
Friedrich Jergitsch and Carmen Redmann Freshfields Bruckhaus Deringer		Catherine Balmond and Katharina Crinson Freshfields Bruckhaus Deringer	
<b>Bahamas</b>	<b>33</b>	<b>European Union</b>	<b>166</b>
Leif G Farquharson and Michelle M Pindling-Sands Graham Thompson		Rachel Seeley and Katharina Crinson Freshfields Bruckhaus Deringer	
<b>Bahrain</b>	<b>42</b>	<b>France</b>	<b>180</b>
Harnek S Shoker Freshfields Bruckhaus Deringer		Fabrice Grillo and Alexandra Szekely Freshfields Bruckhaus Deringer	
<b>Belgium</b>	<b>50</b>	<b>Germany</b>	<b>193</b>
Geert Verhoeven and Satya Staes Polet Freshfields Bruckhaus Deringer		Franz Aleth and Nils Derksen Freshfields Bruckhaus Deringer	
<b>Bermuda</b>	<b>62</b>	<b>Greece</b>	<b>209</b>
Andrew A Martin MJM Limited		Stathis Potamitis and Eleana Nounou PotamitisVekris	
<b>Botswana</b>	<b>68</b>	<b>Hong Kong</b>	<b>221</b>
Kwadwo Osei-Ofei Osei-Ofei Swabi & Co		Georgia Dawson and Look Chan Ho Freshfields Bruckhaus Deringer	
<b>Brazil</b>	<b>73</b>	<b>Hungary</b>	<b>232</b>
Luciana Faria Nogueira and Gabriela Martines Gonçalves TozziniFreire Advogados		Zoltán Varga and Balázs Baranyai Nagy és Trócsányi Law Firm	
<b>Bulgaria</b>	<b>82</b>	<b>India</b>	<b>240</b>
Ina Bankovska and Tsvetelina Stoilova Kinkin & Partners		Nihar Mody and Ankit Majmudar Platinum Partners	
<b>Canada</b>	<b>91</b>	<b>Indonesia</b>	<b>249</b>
Bruce Leonard Chair, The International Insolvency Institute		Herry N Kurniawan, Theodoor Bakker and Ridzky Firmansyah Amin Ali Budiardjo, Nugroho, Reksodiputro	
Craig Mills Miller Thomson LLP		<b>Isle of Man</b>	<b>257</b>
<b>Cayman Islands</b>	<b>101</b>	Stephen Dougherty and Tara Cubbon DQ Advocates	
Andrew Bolton and Andrew Jackson Appleby		<b>Italy</b>	<b>264</b>
<b>China</b>	<b>110</b>	Raffaele Lener and Giovanna Rosato Freshfields Bruckhaus Deringer	
Frank Li, Allan Chen and Rebecca Lu Fangda Partners		<b>Japan</b>	<b>282</b>
<b>Croatia</b>	<b>120</b>	Kazuki Okada, Shinsuke Kobayashi and Daisuke Fukushi Freshfields Bruckhaus Deringer	
Pavo Novokmet and Andrej Skljarov Žurić i Partneri			

<b>Luxembourg</b>	<b>297</b>	<b>Spain</b>	<b>395</b>
Christel Dumont Dentons Luxembourg		Silvia Angós Freshfields Bruckhaus Deringer	
<b>Malaysia</b>	<b>305</b>	<b>Sweden</b>	<b>406</b>
Lee Shih and Nathalie Ker Skrine		Mathias Winge and Henrik Davidsson Setterwalls Advokatbyrå	
<b>Mexico</b>	<b>312</b>	<b>Switzerland</b>	<b>415</b>
Darío U Oscós Coria and Darío A Oscós Rueda Oscós Abogados		Christoph Stäubli* Walder Wyss Ltd	
<b>Netherlands</b>	<b>325</b>	<b>Thailand</b>	<b>429</b>
Michael Broeders and Rodolfo van Vlooten Freshfields Bruckhaus Deringer		Suntus Kirdsinsap, Natthida Pranutnorapal, Piyapa Siriveerapoj and Patinya Sriwatcharodom Weerawong, Chinnavat & Peangpanor Ltd	
<b>Nigeria</b>	<b>341</b>	<b>Turkey</b>	<b>438</b>
Emmanuel Ekpenyong and Cinderella Agunanna Fred-young & Evans LP		Çağlar Kaçar Kaçar, Attorneys at Law	
<b>Norway</b>	<b>348</b>	<b>United Arab Emirates</b>	<b>448</b>
Stine D Snertingdalen and Ingrid E S Tronshaug Kvale Advokatfirma DA		Pervez Akhtar and William Coleman Freshfields Bruckhaus Deringer	
<b>Peru</b>	<b>356</b>	<b>United States</b>	<b>458</b>
Rafael Corzo de la Colina, Renzo Agurto Isla and Lisbeth Benavides Kolind-Hansen Miranda & Amado Abogados		Alan W Kornberg and Claudia R Tobler Paul, Weiss, Rifkind, Wharton & Garrison LLP	
<b>Romania</b>	<b>365</b>	<b>Vietnam</b>	<b>470</b>
Bogdan Bibicu Kinstellar		Thanh Tien Bui Freshfields Bruckhaus Deringer	
<b>Russia</b>	<b>372</b>	<b>Quick reference tables</b>	<b>480</b>
Dmitry Surikov, Maria Zaitseva and Svetlana Tolstoukhova Freshfields Bruckhaus Deringer			
<b>Singapore</b>	<b>386</b>		
Sean Yu Chou, Manoj Pillay Sandrasegara and Mark Choy WongPartnership LLP			

# Preface

## Restructuring & Insolvency 2017

Tenth edition

**Getting the Deal Through** is delighted to publish the tenth edition of *Restructuring & Insolvency*, which is available in print, as an e-book and online at [www.gettingthedealthrough.com](http://www.gettingthedealthrough.com).

**Getting the Deal Through** provides international expert analysis in key areas of law, practice and regulation for corporate counsel, cross-border legal practitioners, and company directors and officers.

Throughout this edition, and following the unique **Getting the Deal Through** format, the same key questions are answered by leading practitioners in each of the jurisdictions featured. Our coverage this year includes new chapters on India, Isle of Man, Malaysia, Norway and Vietnam.

**Getting the Deal Through** titles are published annually in print. Please ensure you are referring to the latest edition or to the online version at [www.gettingthedealthrough.com](http://www.gettingthedealthrough.com).

Every effort has been made to cover all matters of concern to readers. However, specific legal advice should always be sought from experienced local advisers.

**Getting the Deal Through** gratefully acknowledges the efforts of all the contributors to this volume, who were chosen for their recognised expertise. We also extend special thanks to the contributing editor, Bruce Leonard of the International Insolvency Institute, for his continued assistance with this volume.

GETTING THE  
DEAL THROUGH 

London  
November 2016

# Global overview

Richard Tett Freshfields Bruckhaus Deringer

Alan W Kornberg Paul, Weiss, Rifkind, Wharton & Garrison LLP

In this year's global overview, we reflect on business and legal trends that we have seen over the last year.

## Business

### Commodities

For the restructuring world, there are perhaps three particular themes in 2016 up to the early autumn: low commodity prices (especially for oil and gas), low interest rates with generally benign conditions and Brexit.

Having fallen to under \$30 a barrel (Brent) in January 2016, the oil price rallied in the first half of 2016 up to low \$50s in June before dropping back a little. However, this recovery seems to have stalled, with prices still trending below/around \$50 a barrel and remaining less than half their 2014 peak and below the 'break-even' price for many energy producers. Indeed, it shows how dramatically the market has changed when \$50 is a good price and people hope for \$60.

These low oil prices are driving global defaults, which have jumped by 50 per cent since 2015 and hit their highest level since 2009. US corporate defaults and bankruptcies in the energy sector explain much of this rise, with European defaults in oil and gas trending at a much lower level and overall European defaults still below the low term trailing average. Markets are also seeing the pricing pressure in oil and commodities rippling out to groups that derive material revenue from the oil industry - including areas like satellites.

Low commodities prices have also resulted in emerging markets being another area where advisers have been chasing mandates. Russia, Ukraine, Latin America and the like are generating a significant number of ongoing restructurings. The fall from grace of Brazilian telecom giant Oi, which filed for bankruptcy in June, is emblematic of the fortunes of Brazil as the success of the noughties sinks into deep recession. Political and economic fallout from the Petrobras corruption scandal, combined with low commodity prices and rising interest rates, have piled pressure on cash-strapped companies. The same trends are evident across the Latin American economies, which are forecast to shrink again in 2016 after contracting 1.2 per cent in 2015 (Bloomberg). The issues here are extremely serious - as seen most clearly in Venezuela.

### Zombies

Turning to the second theme, while the Fed is nudging rates up, generally interest rates remain low and have been dropping. In the search for stimulus, a number of central banks have even set negative interest rates for deposits (called an act of desperation by some commentators) - most notably the European Central Bank (cut to -0.4 per cent in March 2016) and the Bank of Japan (-0.1 per cent in January 2016). Following the Brexit vote (see more below), the Bank of England has cut the base rate to a record low of 0.25 per cent.

These low interest rates, taken with relatively benign economic conditions and accommodating lenders, are allowing many struggling companies to limp on and on - 'zombie companies'. There remain a good many overleveraged companies that appear to have no prospect to growing themselves into their balance sheets, but which continue to find lenders willing to extend facilities as the 'least bad' option.

### Brexit

One of the shocks of the year was the UK's vote to 'Brexit.' Brexit was heralded with widespread speculation of terrible consequences. It is certainly right that the UK's vote to leave the EU brings great

uncertainty and, for the short to medium term at least, is a negative for the UK, the EU and, indeed, globally. However, thus far, the worries do seem to have been overstated and, as happens so often, in practice the markets go on - albeit with the longer term consequences of Brexit remaining unknown.

It is also worth reminding people that nothing has changed yet. The UK first needs to issue an article 50 notice and, broadly, there follows a two-year period before the exit takes place. The timing for the notice is in the UK government's discretion, and it currently seems likely that the notice will be given in 2017, with an exit in 2019. However, issuing the notice is a political question and, with so many EU member state elections in the next year (including Germany, France and the Netherlands), the EU landscape and the timing of the article 50 notice are unclear.

One of the immediate consequences of the Brexit vote was the slump in sterling to a 31-year low of \$1.29 and it has stayed around \$1.30 since then. However, this is not as low as many predicted, reflecting the negative but 'not so negative' effect of the Brexit vote. As with oil prices, a prolonged slump in sterling will produce winners and losers. Regarding the later, certain sectors, including real estate, tourism and travel (out of the UK), construction and financial services, are particularly exposed to the falling confidence resulting from post-Brexit uncertainty.

Looking to other themes from 2016, the trend towards tougher regulatory enforcement and fines looks set to continue on both sides of the Atlantic though scaling back from the record fines on banks in recent years. The fallout from the LIBOR-rigging scandal continues to bite the financial services industry, with Barclays Bank recently reaching a \$100 million settlement in the US (following its £290 million fine from UK regulators in 2012). Most recently in the US, Wells Fargo & Co, one of the country's biggest banks, was fined \$185 million for allegedly opening over two million unauthorised customer accounts in an effort by bank employees to meet aggressive sales targets and increase bank fees. In the wake of the scandal, the bank fired over 5,000 employees, and its CEO and at least one other senior executive face forfeiting tens of millions of dollars in compensation.

Further, in the US, business filings, predominantly in the energy and commodities sectors but also in other segments, increased over the prior year, and many expect filings to remain steady. Stakeholders' litigation challenges to corporate transactions as a strategy to obtain negotiation leverage continues, increasing the cost, duration and contentiousness of complex corporate restructurings.

### Legislation

As in 2015, restructuring and insolvency law reform is an ongoing theme across all continents. Australia, perhaps in response to being seen as having a relatively unhelpful regime for restructurings, is conducting a wholesale review on barriers to business entries and exits. It is consulting on the introduction of a safe harbour for directors in the wrongful trading regime to strike a better balance between encouraging entrepreneurship and protecting creditors. This chimes with reviews on the corporate insolvency framework that are under way in the EU and separately in the UK, an initial response in the UK being expected by October 2016.

The EU continues to be in reform mode. The Recast Regulation on Insolvency Proceedings takes effect in June 2017 with a view to further

enhancing the existing framework for mutual recognition and cooperation in cross border insolvency matters. Following the Commission Recommendation on a new approach to business failure and insolvency in 2014, the EU has also been seeking views on introducing a harmonised approach to certain insolvency principles and standards across the EU, including early restructuring and second chances. This was expected to result in a new legislative initiative coming out of the EU as early as this year, although it remains to be seen whether Brexit will distract attention from this.

The Netherlands responded to the Commission Recommendation's focus on composition outside insolvency by introducing the 'Dutch scheme', which, after some delays, is expected to go live some time in 2017. Heavily influenced by the English scheme but with the ability to cram down entire classes, it remains to be seen whether the Dutch scheme can challenge the English scheme for pole position among European restructuring tools, especially if the UK does Brexit.

India is preparing for an entirely new insolvency regime to come into force in March 2017. The introduction of 'The Insolvency and Bankruptcy Code' is intended to bring about a shift to a more creditor-friendly regime in the hope of boosting debt markets and should make

insolvencies simpler and much quicker. The proposed changes to the Indian regime are pretty radical, although successful implementation will partially depend on the development of the right culture and judicial infrastructure to support the regime.

Proposed legislation was introduced in the US to address the growing student loan debt, as well as Puerto Rico's financial troubles. US student loans total over \$1.2 trillion and are viewed by many as a potentially significant overhang on near-term US economic growth. Puerto Rico, which owes over \$72 billion to creditors, continues to struggle financially. Given the US political climate in this election year, however, the proposed legislation stalled and none was approved by Congress.

So what will 2017 bring? Global leaders continue to struggle with the economic and social impact of the refugee and migration crisis fuelled by the unrest in the Middle East and elsewhere. On both sides of the Atlantic, there are likely to be major political changes with the US Presidential election in late 2016 and the Dutch, French, German and other EU elections in 2017. How these elections, impacted by the refugee crisis and coupled with the implementation of Brexit, will shape the business and legislative future will be an interesting question for next year's *Getting the Deal Through*.

# Australia

Dominic Emmett and Sabrina Ng

Gilbert + Tobin

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Corporations Act 2001 (Cth) (the Act) is the central piece of federal legislation that governs the registration, administration, insolvency and reorganisation of companies incorporated in Australia. The Act prescribes the manner to administer and regulate the winding up, liquidation, administration and distribution of assets vested in insolvent corporations and other prescribed commercial vehicles.

Section 95A of the Act states that a company is solvent if it can pay its debts as and when they fall due and payable. A company that cannot pay its debts when due and payable – or in other words is not solvent – is insolvent.

The focus in Australian case law is the cash-flow position of the company as opposed to a balance-sheet test. The courts have held that any assessment of solvency should be considered in light of the commercial reality of the company's financial position taken as a whole as opposed to a point in time assessment of the balance sheet taken in isolation.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The Federal Court of Australia and the supreme courts of each state and territory have jurisdiction to hear matters relating to the insolvency of a corporation (both civil and criminal offences arising from insolvency proceedings). Matters pertaining to debt recovery and monetary compensation can also be dealt with by other courts such as district courts, county courts and magistrates' courts within their jurisdictional limits. The judicial institutions have discretion to transfer matters between them if considered appropriate. It is generally only the Federal Court and the supreme courts that have jurisdiction to wind up a company.

Two of the more common forms of insolvency process, voluntary administration and receivership, often have no court involvement.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The Act governs the potential insolvency proceedings of all companies incorporated in Australia and companies incorporated or possessing separate legal personality in foreign jurisdictions that carry on business in Australia along with building societies, credit unions and managed investment schemes.

The provisions of the Act do not govern the potential insolvency proceedings for:

- government agencies;
- state or federal corporate bodies; and
- entities created by statute that are not companies.

The individual statutes creating these bodies will normally provide for their dissolution or winding up.

The following property is generally exempt from the claims of unsecured creditors during the course of a winding-up proceeding:

- property subject to a security interest;
- trust property in which the company has no beneficial interest (if the company is acting as trustee and has a right of indemnity against the trust property for its costs of administering the trust, the proceeds of that indemnity are available to pay the claims of creditors who are owed debts incurred by the trust company in administering the trust); and
- any amount received by a debtor company in respect of insurance taken out against third-party liability, which must be paid to the relevant third party.

Where the company has entered into contracts of reinsurance, the proceeds of those policies are available to meet the company's insurance liabilities as a whole, not just the policy that was reinsured.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There is no precedent in Australia of a government-owned enterprise becoming insolvent. Generally each government-owned enterprise is established under a specific piece of legislation separate to the Act (be it federal or at a state level). This legislation will provide for the winding-up procedure and remedies creditors may have available (noting they are limited compared to a corporate insolvency). Also worth noting is that the test for insolvency is often different under such legislation. As noted, creditors do have remedies, however, as the provisions will vary from enterprise to enterprise, and as there has never been an actual example of these provisions being tested it is difficult to generally comment on how they would work in practice.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No.

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## Secured lending and credit (immoveables)

### 6 What principal types of security are taken on immoveable (real) property?

The principal type of security that is taken on real property in Australia is a mortgage, for which a registration system exists (referred to as the Torrens Title system). Under this system, a mortgagor who has registered a mortgage with the relevant state or territory land title register grants a legal charge over the land as opposed to transferring legal title to the mortgagee. The mortgagor and mortgagee thereafter both possess a legal interest in the land. The mortgagor is free to deal with the land (subject to any restrictions in the terms of the mortgage itself) and retains the beneficial and legal interest in the land. The mortgagee holds a legal charge that will confer actionable rights in the event of default by the mortgagor.

It is also possible under the Australian system for an equitable mortgage over land to exist. This arises in circumstances where the

mortgage is not yet registered but the parties have an intention (often a written agreement) to enter into one or the mortgagor deposits the title deeds with the mortgagee.

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### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

In 2012, the Personal Properties Securities Act 2009 (Cth) (PPSA) came into force in Australia, modelled largely on equivalent legislation in New Zealand and Canada. This legislation consolidated all of the existing registers on which security interests were previously registered and amended many of the concepts and terms associated with taking security over assets.

#### Security interest

The PPSA introduced a uniform concept of a 'security interest' to cover all existing forms of security interests, including mortgages, charges, pledges and liens. It applies primarily to security interests under which an interest in personal property is granted pursuant to a consensual transaction that, in substance, secures payment or performance of an obligation. It also applies to certain deemed security interests such as certain types of lease arrangement for certain terms, retention of title arrangements and transfers of debts, regardless of whether the relevant arrangement secures payment or performance of an obligation. 'Personal property' is broadly defined and essentially includes all property other than land, fixtures and buildings attached to land, water rights and certain statutory licences.

The legislation has introduced a new lexicon relating to security in Australia. For instance, the traditional concept of a fixed and floating charge has now been replaced by 'general security agreement' and the PPSA now determines whether an asset is, in effect, subject to a floating charge on the basis that only circulating assets, as defined by the PPSA, will be treated as being subject to a floating charge for the purposes of other legislation including the provisions of the Act that provide priority of certain claims over floating charge assets. Generally, attachment and perfection of a security interest occurs when the grantor and the secured party execute a security agreement, although the parties can defer attachment, and the security interest is registered on the PPSA register. However, security interests over certain assets can be perfected other than by way of registration, for example, by the security holder controlling the relevant asset in the manner prescribed by the PPSA.

It should be noted that the concept of security interest is broad enough to capture pre-existing forms of security and the documentation creating security has not changed significantly (ie, charges, debentures, mortgages and pledges may still be used with certain amendments).

One of the most significant changes implemented by the PPSA is to require the registration of retention of title arrangements in order to protect a supplier's title to the relevant supplied goods.

If a security interest is not perfected in accordance with the PPSA the security interest will, on liquidation of the grantor, vest in the grantor. This has created a paradigm shift for retention of title arrangements since failure to perfect the retention of title arrangement (by registration) will vest title in the relevant goods in the recipient of the goods, despite the agreement between supplier and recipient that the supplier retains title to those goods until they are paid for.

#### Non-PPSA property

The PPSA does not cover security interests in land or fixtures and buildings attached to land and a mortgage over real property must be registered under the Torrens Title system, which operates under Australian law by registration on the relevant state or territory land title register (see question 5).

There are also certain assets such as statutory licences (such as mining licences), which, by virtue of statute, are expressed to be outside the operation of the PPSA and any security interest over any such asset is governed by common law.

There have been limited cases before the courts dealing with the PPSA, and so at this stage the New Zealand and Canadian authorities provide instructive (but non-binding) authority in respect of the interpretation of the PPSA.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

A creditor may commence proceedings through the courts to recover outstanding amounts owing by a recalcitrant debtor company. A creditor, at the same time, may also request that the court order injunctive relief to freeze the assets of the company if there is a risk of assets or value being dissipated. A failure to plead a substantive defence will generally enable a default judgment to be granted and the creditor may, after this, take steps to wind the debtor company up.

The court has extensive powers to compel compliance and enforce a range of remedies including seizure of assets, diversion of a debtor company's income and orders for winding up of the company. In relation to special procedures, the relevant rules of court provide that foreign creditors may be required to provide security for costs (ie, a sum of cash to the courts) of enforcing a judgment in Australia.

The options available to unsecured creditors of an insolvent company or company in distress are limited. Once a company is placed into administration or liquidation, a statutory moratorium will apply to any proceedings commenced, including any enforcement proceedings. The statutory moratorium is addressed in greater detail in question 15.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Under the Act both the members of the company and also the creditors have the option under certain circumstances to commence a voluntary winding up of a company. Neither procedure requires court sanction. The determinative factor for which voluntary regime may be pursued is the company's solvency position.

#### Members' voluntary winding up

A members' voluntary liquidation is a solvent winding up. It requires that the directors of the company make a declaration of solvency under section 494 of the Act. The declaration of solvency requires that the directors of the company to form the opinion, after an inquiry into the affairs of the company, that the company will be able to discharge its debts in full within 12 months of the commencement of winding up. This is coupled with a special resolution (ie, at least 75 per cent of votes cast by members entitled to vote on the resolution) of the members to wind up the company. Subsequently, a copy of this resolution must be lodged with the Australian Securities and Investments Commission (ASIC) within seven days, to be published in the gazette within 21 days.

#### Creditors' voluntary winding up

A creditors' voluntary winding up arises when the company is in fact insolvent. It can occur in a numbers of circumstances, including:

- if the members of the company by special resolution resolve that the company be wound up and the directors cannot provide a solvency declaration. In these circumstances the liquidator appointed is obliged to convene a creditors' meeting within 11 days of the day of the passing of the special resolution. At the meeting of creditors, the creditors may resolve to appoint a different liquidator, and also appoint a committee of inspection, being a representative group of creditors;
- in situations where a liquidator appointed by the members forms the opinion that the company is in fact insolvent will convert the process from a members' voluntary winding up into a creditor's voluntary winding up; and
- a company may also enter a creditors' voluntary winding up at the end of an administration if the creditors resolve to at the second creditors' meeting.

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Under Australian law a compulsory liquidation will involve application to and orders from the court. A creditor or other eligible applicant must lodge an application with the court to wind up a company. On an

application to wind up the company in insolvency, the creditor must show that the company is unable to pay its debts as and when they fall due.

There are two situations in which a company will be held to be unable to pay its debts:

- if the company has not paid a claim for a sum due to a creditor exceeding A\$2,000 within 21 days of service of a prescribed written statutory demand (the Act sets out specific requirements); or
- if it is proved to the court as a question of fact that the company is unable to pay its debts as they fall due.

Grounds are also available for a creditor to apply to the court for winding-up orders against a company not necessarily related to solvency, including that it is 'just and equitable' to do so or because of a deadlock at a shareholder or director level affecting the ability to manage the company.

After a winding-up order, management of the company is removed from the directors and the company will likely cease as a going concern (except as is necessary to proceed with the winding up). The liquidator appointed will take control of the affairs of the company and his or her duties include realising the company's assets for the benefit of the creditors.

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## Voluntary reorganisations

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### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

#### Voluntary administration

The purpose and operation of voluntary administration is outlined in Part 5.3A of the Act. Voluntary administration has been compared to the Chapter 11 process in the United States, however, unlike the Chapter 11 process voluntary administration is not an in situ debtor process. In a voluntary administration the creditors control the final outcome to the exclusion of management and members. The creditors ultimately decide on the outcome of the company, and in practice it rarely involves returning management back to the former directors.

The purpose of Part 5.3A is to either:

- maximise the chances of the company, or as much as possible of its business, continuing in existence; or
- result in a better return for the company's creditors and members than would result from an immediate winding up, if it is not possible for the company or its business to continue in existence.

An administrator may be appointed in three possible ways under the Act:

- by resolution of the board of directors that in their opinion the company is, or is likely to become, insolvent;
- a liquidator or provisional liquidator of a company may, by writing, appoint an administrator of the company if he or she is of the opinion the company is, or is likely to become, insolvent; and
- a secured creditor who is entitled to enforce security over the whole or substantially whole of a company's property may, by writing, appoint an administrator if the security interest is over the property and is enforceable.

An administrator has wide powers, and will manage the company to the exclusion of the existing board of directors. Once an administrator is appointed, a statutory moratorium is activated that restricts the exercise of rights by third parties under leases and security interests and in respect of litigation claims, which is designed to give the administrator the opportunity to investigate the affairs of the company, and either implement change or be in a position to realise value, with protection from certain claims against the company. A secured creditor with security over whole or substantially whole of the assets of the company has 13 business days following the appointment of the administrator to exercise right under the security granted in its favour (ie, appoint a receiver).

There are two meetings over the course of an administration critical to the outcome of the administration. Once appointed, an administrator must convene the first meeting of creditors within eight business days (at such meeting the identity of the voluntary administrator is confirmed, the remuneration of the administrator is approved and a committee of creditors may be established). The second creditors' meeting

is normally convened 20 business days after the commencement of the administration (this may be extended by application to the court). At the second meeting the administrator provides a report on the affairs of the company to the creditors and outlines the administrator's views as to the best option available to maximise returns. There are three possible outcomes that can be put to the meeting:

- enter into a deed of company arrangement (DOCA) with creditors (discussed further below);
- wind the company up; or
- terminate the administration.

The administration will terminate according to the outcome of the second meeting (ie, either by progressing to liquidation, entry into a DOCA or returning the business to operate as a going concern (although this is rare)). When the voluntary administration terminates, a secured creditor that was estopped from enforcing a security interest because of the statutory moratorium becomes entitled to commence steps to enforce that security interest unless the termination is because of the implementation of a DOCA approved by that secured creditor.

#### DOCA

A DOCA is effectively a contract or compromise between the company and its creditors. Although closely related to voluntary administration, it should in fact be viewed as a distinct regime, where the rights and obligations of the creditors and company differ from those under a voluntary administration.

The terms of a DOCA may incorporate that which make its operation similar to a voluntary administration (giving similar rights to a deed administrator as a voluntary administrator), but may also provide for, inter alia, a moratorium of debt repayments, a reduction in outstanding debt and the forgiveness of all, or a portion of, the outstanding debt. It may also involve the issuance of shares, and can be used as a way to achieve a debt-for-equity swap.

Entering into a DOCA requires the approval of a bare majority of creditors both by value and number voting at the second creditors' meeting. A DOCA will bind the company, its shareholders, directors and unsecured creditors. Secured creditors do not need to vote at the second creditors' meetings and only those who voted in favour of the DOCA at the second creditors' meeting are bound by its terms. Unlike a scheme of arrangement, court approval is not required for a DOCA to be implemented provided it is approved by the requisite majority of creditors.

Upon the execution of a DOCA the voluntary administration terminates. The outcome of a DOCA is generally dictated by the terms of the DOCA itself. Typically, however, once a DOCA has achieved its goal it will terminate. If a DOCA does not achieve its goals or is challenged by creditors it may be terminated by the court.

#### Schemes of arrangement

A scheme of arrangement is a restructuring tool that sits outside of formal insolvency: the company may become subject to a scheme of arrangement whether it is solvent or insolvent.

A scheme of arrangement is a proposal put forward (with input from management, the company or its creditors) to restructure the company in a manner that includes a compromise of rights by any or all stakeholders. The process is overseen by the courts and requires approval by all classes of creditors. The pre-existing management remains in control of the company during the process (and also depending on the terms of the scheme itself after its implementation). In recent times schemes of arrangement have become more common, in particular for complex restructures involving debt for equity swaps in circumstances where the number of creditors within creditor stakeholder groups may make a contractual and consensual restructure difficult.

A scheme of arrangement must be approved by at least 50 per cent in number and 75 per cent in value of creditors in each class of creditor. Classes are determined by reference to commonality of legal rights and only those creditors whose rights will be affected, compromised or amended by the scheme need be included. It must also be approved by the court in order to become effective.

The outcome of a scheme of arrangement is dependent on the terms of the arrangement or compromise agreed with the creditors, but most commonly, a company is returned to its normal state upon

implementation as a going concern but with the relevant compromises having taken effect.

The scheme of arrangement process does however have a number of limiting factors associated with it, including cost, complexity of arrangements (ie, class issues), uncertainty of implementation, timing issues (ie, because of various procedural requirements for holding the meetings, and as it must be approved by the court it is subject to the court timetable and can only be expedited to a certain extent) and the overriding issue of court approval (ie, a court may exercise its discretion to not approve a scheme of arrangement, despite a successful vote, if it is of the view that the scheme of arrangement is not equitable).

These factors explain why schemes of arrangement tend only to be undertaken in large corporate restructures and in scenarios with sufficient time for execution and implementation to accommodate the procedural and courts' requirements.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

##### Receivership

Unlike the United Kingdom receivership is still an option available to secured creditors in Australia. Receiverships, particularly coordinated appointments at a holding company level, can and have been used to effect corporate restructures and reorganisations.

There are two ways in which a receiver or receiver and manager may be appointed to a debtor company. The most common manner is pursuant to the relevant security document granted in favour of the secured creditor when a company has defaulted and the security has become enforceable. Far less common in practice is the appointment of a receiver pursuant to an application made to the court. Court appointments are normally done to preserve the assets of the company in circumstances where it may not be possible to otherwise trigger a formal insolvency process. However, given the infrequency of court-appointed receivers this article focuses on privately appointed receivers.

For a privately appointed receiver the security document itself will entitle a secured party to appoint a receiver, and will also outline the powers available (supplemented by the statutory powers set out in section 420 of the Act). Generally, a receiver has wide-ranging powers including the ability to operate, sell or borrow against the secured assets. The appointment is normally effected contractually through a deed of appointment and indemnity, and the receiver will be the agent of the debtor company, not the appointing secured party.

On appointment a receiver will immediately take possession of the assets subject to the security. Once in control of the assets the receiver may elect to run the business if the receiver is appointed over all or substantially all of the assets of a company. Alternatively, and depending on financial circumstances, a receiver may engage in a sale process immediately. While engaging in a sale process a receiver is under a statutory obligation to obtain market value, or in the absence of a market, the best price obtainable in the circumstances. This obligation is enshrined in section 420A of the Act. It is this duty that has traditionally posed the most significant stumbling block to the adoption of prepackaged restructure processes through external administration. Often referred to a 'prepack', this is where a restructuring is developed by the secured lenders prior to the appointment of a receiver and is implemented immediately or very shortly after the appointment is made. This is because of the concern that a prepackaged restructuring that involves a sale of any asset without testing against the market could be seen to be in breach of the duty under section 420A. Sales processes conducted immediately prior to appointment or the potential for immediate dilution of value are increasingly facilitating receiver-ship sales without a full testing of the market.

Once a receiver has realised the secured assets and distributed the net proceeds to the secured creditors (returning any surplus to subordinated security holders or the company) he or she will retire in the ordinary course.

##### Voluntary administration

As referred to in question 11 a secured creditor can often appoint an administrator to force a reorganisation as an alternative to exercising its security. Once the voluntary administration occurs the creditors are in control of the company's fate (including any restructuring

or reorganisation) and the success of which will be dependent on the relevant majority, by number and dollar value, voting in favour of it. The effects of this procedure are referred to above under 'voluntary administration'.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

When a company is insolvent or likely to become insolvent its board of directors can appoint a voluntary administrator under Part 5.3A and the appointment itself is a defence under the Act to insolvent trading. There is, however, no explicit statutory provision obliging companies to commence such insolvency proceedings. Directors have a duty under the Act to prevent insolvent trading. If a company enters into liquidation Part 5.7B, division 4 makes directors who breach this duty liable to compensate the company for all new debts incurred from the time a company is found to have become cash-flow insolvent. Therefore, a director may suffer civil or criminal liability for insolvent trading where he or she knew, or had reasonable grounds for suspecting, that the company was insolvent or would become insolvent. These provisions are intended to compel directors to take active steps (such as the appointment of a voluntary administrator) in an expeditious manner, thereby protecting members and creditors from the continuation of insolvent businesses.

In addition to the potential liability of directors, should the company continue to carry on business while insolvent, certain transactions the company enters into with third parties may be subject to challenge and ultimately be held to be void should the company formally enter into liquidation (for example, unfair preference or uncommercial transaction). See question 39 for further information.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

During an informal reorganisation or formal scheme of arrangement, the ability of a debtor company to carry on its business will depend upon the terms of agreement with its creditors.

This position differs, however, if the restructuring occurs within the context of a receivership or an administration. Control of the company is transferred from the directors to the administrator or receiver. An administrator has wide-ranging powers to carry on the business of the company where that is consistent with the purpose of the administration, whereas a receiver has wide-ranging powers provided for under the Act and the security agreement itself.

For the purposes of carrying on the business, the administrator has the power under section 437A to pay creditors who supply goods or services to the company after the company has gone into administration in preference to ordinary unsecured creditors. The administrator must report periodically to creditors to seek approval for proposals embarked upon in furtherance of the administration. The creditors may appoint a creditors' committee to supervise the administration. Administrators may apply to the court for directions regarding the manner in which to conduct the administration. Creditors may also apply for relief against the administrator, which could involve removal.

A receiver may continue to run the business as a going concern with a view to maximising the return available to the secured creditor. Services engaged (including the providers of goods and services) are treated as costs of the receivership and the preferential payment of such costs is provided for in the appointment document. The sale of the assets of the business is addressed in question 18.

Generally after formal insolvency proceedings are commenced the power and roles of company officers are at the discretion of the insolvency administrator appointed (receiver, administrator or liquidator)

who is ultimately responsible for those roles (for example, carrying on the business of the company). In an informal workout where there has been no formal appointment the company officers continue to be able to exercise all powers unless otherwise agreed with creditors.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

##### Receivership

During a receivership no moratorium exists, and creditors may take action against the company including initiating court proceedings, but such actions are treated as unsecured claims (subordinated to the claims of the secured creditors who appointed the receiver). The receiver is likely to be in control of the company's material assets and is permitted to realise such assets for the benefit of the secured creditor only (any surplus is provided to the company and would be available for distribution to unsecured creditors).

##### Voluntary administration

The Act provides for a moratorium over legal proceedings as an automatic consequence of a company entering into voluntary administration. Consequently, no legal proceedings can be initiated or proceeded with except with the administrator's written consent or leave of the court. An exception, however, is made in the case of criminal proceedings.

##### Liquidations

After the commencement of a winding up of a company, or after appointment of a provisional liquidator, legal proceedings are not to be commenced or continued against a company without leave of the court, pursuant to section 471B of the Act. Secured creditors are generally granted immunity from this process by section 471C, assuming the validity of their security, as they remain entitled to realise their security despite the liquidation.

Where a statutory moratorium exists, while not determinative, a court is more likely to grant leave for a claimant to proceed against the company if there is a public interest aspect to the claim, such as in the case of claims brought by regulators for statutory breaches, or where the claimant will have access to insurance proceeds.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

##### Voluntary administration

A voluntary administrator is given the power under section 437A of the Act to manage the affairs of the company and to raise loans on security over company assets to carry on the business of the company. The repayment of this credit is treated as an expense of the administration and is given statutory priority over ordinary unsecured creditors.

##### DOCA

Whether a deed administrator has the power to raise loans will depend on the terms of the DOCA. The repayment of this credit will usually be treated as an expense of the deed administration and will be given priority distributions to creditors.

##### Liquidation

Liquidators are expressly permitted to obtain credit under section 477, whether on the security of company property or otherwise, as far as is necessary for the beneficial disposal or winding up of the company. Such credit will have priority over ordinary unsecured creditors but only in respect of the new funds and up to the value of the security.

##### Receivership

The terms of the appointment document and section 420 of the Act provide receivers with wide-ranging powers (including the ability to borrow). Such borrowings are treated as expenses of the receivership

and are provided priority, or alternatively the original security document may provide that such financing is to be afforded the same priority as the first-ranking security.

### Schemes of arrangement

Obtaining financing and use of assets as security in a scheme of arrangement and informal voluntary reorganisations is solely a matter for agreement between the company and its creditors.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

##### Liquidation

Set-off refers to the right of a creditor to plead a debt due from the debtor as a defence to all or part of the debtor's claim made against it. Section 553C of the Act provides that statutory set-off is available in a liquidation scenario where there has been a mutual dealings between the distressed company and relevant creditor. In such circumstances an automatic account is taken of the sum due from the one party to the other in respect of those mutual dealings and the sum due from the one is to be set off against any sum due from the other.

Only the balance of the account is admissible as proof against the company or is payable to the company. The Act allows a broad range of claims to be capable of set-off. The rule entitles creditors who are also debtors to have preference over the general body of creditors. Only unsecured creditors and secured creditors that choose not to rely on their security may take advantage of the rule.

A creditor is, however, unable to claim the benefit of set-off if he or she had, at the time of the relevant transaction, notice of insolvency of the company. Further, a creditor cannot offset any existing claim or debt of the company against new claims or debts that may arise during the period of administration.

##### Other reorganisations

In other reorganisations, there is no statutory right of set-off and the creditor must rely on any contractual rights they may have. Those rights will be subject to a statutory lien that has attached to the company's property at the time that the set-off is made. In practice, however, administrators and deed administrators will recognise set-off as if section 553C did apply as generally creditors can claim prejudicial treatment if they receive less from administrators or under DOCAs than they would under a liquidation scenario.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

##### Receivership

As noted, a receiver is under a statutory obligation to obtain market value or, in the absence of a market, the best price obtainable in the circumstances under section 420A of the Act. Upon a sale the receiver will transfer the assets free of security interests (a release will be provided by the appointing secured creditor) and often the terms of any intercreditor arrangements will provide for the automatic release of subordinated security. In circumstances where an automatic release mechanism is not provided for, direct negotiations will need to take place with the secured subordinated creditors.

##### Voluntary administration

A voluntary administrator may sell assets, noting, however, it is not permitted to sell assets subject to security without consent (normally, a receiver will be appointed and have control over such assets). Administrators can apply to the court if such consent is not given and

the court may make an order if it is satisfied that the secured creditor is adequately protected.

### Liquidations

Liquidators appointed in the context of either voluntary or compulsory liquidations can sell or otherwise dispose of unencumbered property of the company without needing to seek approval from the court or other parties to the liquidation. The purchaser will acquire the assets unencumbered unless there are debts or liabilities passing to the purchaser as provided for in the sale documentation. If assets are encumbered, consent of the encumbrancer will be required unless a court directs otherwise.

A liquidator owes fiduciary duties to the company. In realising company property, a liquidator (or administrator) has a duty to obtain the highest possible price for the assets of the company, keeping in mind that the winding up should not be unnecessarily protracted. Property may be sold in any way the liquidator deems fit, including private contract and, usually, public auction. While creditors may purchase assets of the company, the purchase price will not be able to be set off against the debt owed to the creditor by the company. Instead, any funds raised by the sale of company property will be for the benefit of the creditors as a whole, to be distributed according to the relevant distribution rules.

### Schemes of arrangement

The terms of the scheme itself will provide for the disposal of assets and any associated release of security required. Such releases will not be automatic, however, and will need either agreement from the creditors or the provision of such release in associated finance and security documents.

### Informal reorganisations

In an informal reorganisation of a company the conditions of the reorganisation and sale or use of assets are as negotiated with the relevant creditors.

### Stalking horse bids

While there is nothing to prevent stalking horse bids, they seldom occur in the Australian context.

### Credit bids

Credit bids are permissible under Australia law and generally a means of pursuing loan-to-own strategies. The offer will be assessed in light of the relevant sales process conducted and the nature of the insolvency administration the company is subject to. Courts generally have limited involvement in assessing a credit bid (save as part of a scheme of arrangement or where a sale has been challenged). In such circumstances the court will scrutinise the credit bid in light of the situation generally as well as against other proposals received and in light of any sale process run (if required). There would be no prohibition on an assignee of the original secured creditor making a credit bid (provided the assignment was valid under law).

### Intellectual property assets in insolvencies

**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

Pre-existing contractual arrangements will govern a licensor's ability to terminate a debtor's entitlement to use intellectual property. There is no ipso facto protection afforded under Australian law.

A company administrator's power under section 437A to carry on and manage the property of the business extends to the use of intellectual property granted under an agreement with the debtor. Likewise, a receiver, in the absence of a licensor exercising termination rights, may also continue to use intellectual property.

### Personal data in insolvencies

**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

There are no restrictions on the use of personal information or customer data that apply in an insolvency that would not have otherwise applied to use by the company in a solvent context. For example, while there are restrictions against the use of personal information under Australian privacy laws, those laws will generally not prevent the transfer of that information to a purchaser as part of the sale of the company's business.

A company administrator's power under section 437A to carry on and manage the property of the business extends to the use of customer data collected by the company in its business. Likewise, a receiver, in the absence of specific contractual terms to the contrary, may also continue to use customer data collected by the company in the course of the business.

### Rejection and disclaimer of contracts in reorganisations

**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

Liquidators are given the specific ability to disclaim property or uncommercial contracts under Part 5.6, division 7A of the Act. A liquidator can, subject to objections being made to the court by aggrieved parties, disclaim onerous property in writing. Court approval is required for disclaiming contracts as this is likely to adversely affect third-party interests. There are no specific provisions for disclaimers in a voluntary liquidation, although the court has wide powers to control these reorganisations and application can be made to the court.

Receivers and administrators are not given specific powers to disclaim contracts, they may, however, look to ignore contracts with any resulting damages claim being unsecured against the company (not the receiver or the administrator personally).

If the debtor (either acting by the insolvency administrator appointed or otherwise) breaches the contract after formal insolvency has commenced then the aggrieved counterparty has all remedies available to it under contract law (including claim for damages and any right to terminate). Any such damage will be an unsecured claim as against the debtor company itself and only in very limited circumstances will an order for specific performance be made against the debtor company.

### Arbitration processes in insolvency cases

**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

There are no restrictions under Australian law preventing a distressed company or its creditors from pursuing alternative dispute resolution options, such as arbitration or mediation. The success or willingness to engage in these procedures will obviously be dictated by the parties involved. These arrangements, however, are not without their limitations. For example, there is no obligation on creditors to agree to an informal arrangement and any one creditor can veto a proposed arbitration or mediation outcome if its rights with regard to the others creditors are directly affected (or act outside its restrictions). Its non-binding nature provides sufficient disincentive for creditors to consider these procedures, and it is rarely seen.

It should be noted that courts will generally allow arbitration proceedings to continue while insolvency proceedings remain open to aid the just and expeditious resolution of creditors' claims.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

A scheme of arrangement must be approved by a majority of creditors voting on the resolution and holding at least 75 per cent in value and 50 per cent in number of voting creditors in each class. If approved by the creditors, supplementary approval by the court is required at the second court hearing. Schemes of arrangements may provide for the release of third parties (as opposed to DOCAs where the courts have held it is not possible).

In the context of a voluntary administration, creditors may resolve that the company should execute a DOCA. The company must execute the instrument within 15 business days of such a resolution. A DOCA can be varied by either a subsequent resolution of creditors or by the court. A validly passed DOCA binds all unsecured creditors, regardless of whether they voted in favour of the DOCA. The administrator, in recommending that the creditors enter into a DOCA, is required to provide creditors with sufficient information about the proposed arrangement when giving notice of the second meeting. Entitlements of employees must be provided the same level of priority in a DOCA as in a winding up, unless the employees agree otherwise.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

The voluntary administration regime was introduced into the Act to provide distressed companies with a process to initiate an expedited reorganisation without court approval. A voluntary administrator is required to complete the investigations relating to the company's business, property, affairs and financial circumstances about four to six weeks after his or her appointment. The administrator is then required to convene a creditors' meeting at which the administrator provides the creditors with a detailed report of the investigation and recommendations. The creditors then decide between three alternatives: to execute a DOCA, to wind up the company or to end the administration.

As to receivership, see question 12.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A scheme of arrangement may either be defeated by a creditors' vote or not be sanctioned by the court. Should either of these occur, there is no automatic process that occurs, rather the company reverts back to its pre-existing state (which may include financial difficulties).

A proposed reorganisation through a DOCA may be defeated by a majority of creditors at the second meeting. At such meeting the creditors may vote for the company to be wound up or to give back the control of the company to the directors, thus ending the administration, rather than executing a DOCA. Further, if the company fails to execute a DOCA within 15 business days of a successful resolution at a second creditors' meeting, the company will enter into a creditors' voluntary winding up. Once executed, if there is a material contravention of the DOCA by the debtor company, a creditor or other interested person may apply for the termination of an executed DOCA by an order of the court. If an order is granted, the company again enters into a creditors' voluntary winding up.

An aggrieved creditor might also look to terminate a DOCA on the grounds of unfair prejudice.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

##### Voluntary administration

Notice of the appointment of an administrator must be lodged with ASIC within one day and creditors must be notified of the appointment within three days.

The administrator must convene a meeting of creditors within eight business days of his or her appointment. Notice of this meeting must be given in writing to as many creditors as is reasonably practicable at least five business days before the meeting and published in a public newspaper. At this meeting, creditors have the opportunity to appoint a different administrator and may also decide whether to appoint a consultative committee of creditors to assist the administrator. Although the committee cannot give directions to the administrator, it can compel the administrator to report on matters relating to the administration. The committee is also in a fiduciary relationship with the creditors and thus cannot profit from their role.

The second creditors' meeting must be convened by the administrator within five business days after the 'convening period'. The convening period is 20 business days from the date the administration begins and the same notice requirements apply. This is extended to 25 business days if the administration begins in December or occurred less than 25 days before Good Friday. The notice of the meeting must be accompanied by a report setting out the company's business, property, affairs and financial circumstances and a statement expressing the administrators' opinion on each of the options available to the creditors (executing a DOCA, returning control of the company to the directors or winding up the company). If the administrator proposes a DOCA, details of the proposed DOCA must also be provided. At the meeting, the creditors decide and vote on which of the three available options they wish to pursue. The administrator presides at both the first and second meetings.

The reporting obligations of an administrator include the following:

- lodge notice of appointment with ASIC by the next business day following appointment, and advertise appointment within three business days;
- prepare and lodge a report with ASIC where it is suspected that an officer, employee or member of the company has committed an offence in relation to the company; and
- where the creditors vote to wind up the company, to lodge a copy of that resolution with ASIC within five business days of it being passed.

##### Creditors' voluntary winding up

In the event of a creditors' voluntary winding up the liquidator of the company is obliged to convene a creditors' meeting within 11 days of the day of the passing of the special resolution to wind the company up. The liquidator must give creditors at least seven days' notice of the meeting. The notice must contain a summary of the affairs of the company and a list setting out the names of all creditors, the addresses of those creditors and the estimated amounts of their claims as shown in the records of the company. The liquidator must advertise the creditors' meeting at least seven and no more than 14 days before the meeting. At the meeting of creditors the creditors may resolve to appoint a different liquidator, and also appoint a committee of inspection. They will also be called upon to approve the liquidator's remuneration.

The reporting obligations of a liquidator of a creditors' voluntary winding up include the following:

- lodging with ASIC, at least seven days before the meeting, a copy of the notice given to creditors and all accompanying documents;
- publishing notice of the resolution in the Gazette within 21 days of passing a resolution to wind the company up; and
- lodging with ASIC the minutes of the meeting of creditors within one month.

In the event of a creditors' voluntary winding up, if the winding up of the company lasts for more than one year the liquidator is required to call a meeting of the creditors. At this meeting the liquidator must provide an account of the liquidator's acts and dealings in relation to the winding up of the company in the previous year. In both types of winding up, committees of creditors can be formed. They can approve fees and remuneration and advise the liquidator of the views of the general body of creditors.

### Receivership

During a receivership there is no obligation to call a creditors' meeting, but notice of the appointment must be lodged with ASIC. Reports must be lodged with ASIC during the course of the receivership and notification must be given on its termination.

### Third-party releases

Only a scheme of arrangement can provide for the release of liabilities owed by third parties who are not part of the debtor group. The case of *Lehman Brothers Australia Ltd*, in the matter of *Lehman Brothers Australia Ltd (in liq)* (No. 2) [2013] FCA 965 confirmed this position. This case involved approving a scheme that provided for the release of creditors' claims against the company's insurers.

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### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

An administrator, liquidator or provisional liquidator can sell or otherwise dispose of, in any manner, all or any part of the property of the company. As a claim available to an estate forms part of the company's property, a liquidator may assign the claim to a creditor for consideration. The beneficiary of the 'fruits of the remedies' is thus dependent upon the terms of the assignment. When the liquidator is without funds, creditors may provide an indemnity or funding to the liquidator so that apparently meritorious claims may be pursued for the benefit of all creditors. In such circumstances, the creditors providing the indemnity or funding may be entitled to receive a higher dividend than they would otherwise receive by operation of section 564 of the Act (see question 31).

In addition to administrators' and liquidators' power to assign causes of action, third-party litigation funding has been increasing in acceptability and prevalence since the endorsement of the practice in the non-insolvency context by the High Court of Australia in *Campbells Cash and Carry Pty Ltd v Fostif Pty Ltd* (2006) 229 CLR 386. This has brought with it increased access to litigation funding for liquidators and administrators, and more recently the receivers of the Brisconnections group of companies have accessed third-party funds to bring proceedings against the traffic forecaster.

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### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Committees in the Australian insolvency regime are creatures of statute and are not seen in the context of representing creditor stakeholder groups as they might be in the United States.

At any stage during the winding up, the members or creditors of the company may request that a committee of inspection be appointed. In such a case, the liquidator must call separate meetings of creditors and members for the purpose of determining whether a committee of inspection should be appointed and, if a committee is to be appointed, the numbers of creditors and members to be appointed and the persons who are to be members of the committee.

The role of the committee of inspection is to supervise and assist the liquidator. Examples of the types of direction the committee may make include approving the remuneration of the liquidator, approving the institution of legal proceedings on behalf of the company, and directions as to the compromise of debts owing to the company. Committees of inspection are most often used in large liquidations where it is difficult for the liquidator to engage with the entire body of creditors on a regular basis.

The committee must have at least two members, drawn from the body of creditors and members. A company can be a member, acting through an authorised agent. Generally, the members of the committee of inspection will comprise those with a substantial interest in the winding up of the company, such as large creditors and members holding a large proportion of the company's shares.

The liquidator of the company must have regard to the directions of the committee, but the creditors or members have the power to override the committee's directions.

Members of the committee of inspection owe the general body of creditors and members fiduciary duties and therefore must act in the best interests of the creditors and members rather than for their own benefit.

There is no statutory provision governing the remuneration of the committee of inspection. Except with leave of the court a committee member may not derive any income from their position. They also must not become the purchaser of any property of the company.

At the first meeting of creditors during held during a voluntary administration a committee of creditors may be established. This committee's main role is to consult with the administrator and to receive and consider reports by the administrator. A committee of creditors can reasonably request reports, but unlike a committee of inspection in a liquidation, it cannot give directions to the administrator.

It is almost unheard for such committees to retain counsel and advisers.

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### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

##### Identity

In insolvency proceedings involving corporate groups, a consolidated group is not considered as a single legal entity. Where companies operate as a consolidated group, the starting legal position is the 'separate personality' principle prevents creditors of an insolvent company from gaining access to the funds of other companies for payment of their debts.

The Act, however, provides for a holding company to be liable for the debts of their insolvent subsidiaries in certain circumstances. These provisions enable the subsidiary's liquidator to recover amounts equal to the loss or damage suffered by creditors from the parent company if the parent failed to prevent the subsidiary from incurring debts while there were reasonable grounds to suspect that the subsidiary was insolvent.

The corporate veil may also be lifted in circumstances where an insolvent subsidiary is deemed to be acting as a mere agent, conduit or partner of its parent company. Australian courts have, however, displayed greater reluctance than their UK counterparts to lift the corporate veil in these circumstances.

The only form of external administration that expressly permits combining proceedings by parent and subsidiary companies is under a scheme of company arrangement. To enable a scheme, an application must be made to the court requesting a meeting of the creditors and members (refer to question 10). Where a scheme of arrangement is proposed involving a large corporate group the application may request for the meeting to occur on a consolidated basis. An application for an order to transfer the whole of the assets and liabilities of the subsidiaries to the parent company may also be made when seeking approval of a proposed scheme.

This scheme requires significant court involvement and thus execution is generally slower and more expensive than voluntary administration.

##### Pooling

Pooling of group funds may occur in limited circumstances, as prescribed by Division 8 of Part 5.6 of the Act, being sections 571 to 579L. Generally, those circumstances are where there is a substantial joint business operation between members of the same corporate group and external parties, such that members of the group are jointly liable to

creditors. The liquidator of the corporate group being wound up makes what is called a pooling determination, after which separate meetings of the unsecured creditors of each company must be called to approve or reject the determination. The court may vary or terminate any approved pooling determination.

In relation to a company in liquidation, the court may make orders for the transfer of assets from a winding up in Australia to an external administration outside Australia, either pursuant to section 581 of the Act or pursuant to the UNCITRAL Model Law, incorporated into Australian law by the Cross-Border Insolvency Act 2008 (Cth).

## Appeals

### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

An appellant will have an automatic right of appeal against any final decision of a court. A final decision of the court might include an order to wind up a company, an order to appoint a receiver or an order to set aside a DOCA.

An appellant will need to seek leave of the court to appeal any intermediate decision of the court (ie, a decision that is made along the way to the court making a final decision). An intermediate decision of the court might include orders relating to the timetabling of proceedings or in relation to jurisdictional issues or issues of standing.

An appellant may be required to post security to proceed with an appeal at the application of the respondent. A court is more likely to order that security be posted if the appellant does not have assets in Australia or is impecunious. The amount of security will be based on the costs that the respondent may recover in the event that the appellant is unsuccessful.

## Claims

### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

A liquidator appointed will notify creditors of the submission date and may do so by advertising it in a newspaper and also on the centralised insolvency notice website. This date may not be less than 14 days after the date of notice given to the creditors. Once the particulars of a debt are submitted by a creditor, the liquidator may admit all or part of the claim; reject all or part of the claim; or require further evidence to be submitted in support of it. If further evidence is required, the liquidator must notify every creditor in writing of the day on which the formal proof must be submitted. A liquidator must deal with submitted formal proof of claims within 28 days of receipt.

Where a proof of debt is rejected by a liquidator, grounds for the rejection must be provided to the creditor within seven days. A creditor can appeal the liquidator's decision in court within the time specified in the notice (at least 14 days after service).

It is possible for a creditor's claim to be assigned and such assignment must be in writing. An assignee may apply to the liquidator and the court to have its new proof of debt stand as substituted for the assignor's proof of debt. Such an assignee will be able to enforce the full value of the claim irrespective of whether it was acquired at a discount (ie, below par).

Claims for contingent debts are admissible in the winding up of a company. When a proof of debt is contingent in nature, the liquidator may either make an estimate of the value of the debt or claim as at the date of winding up, or refer the question to the court for judicial consideration. A creditor aggrieved with the estimate made by the liquidator may appeal to the court. If the contingent event occurs after the date of winding up, the creditor is entitled to prove for the actual amount of the claim.

A creditor can claim for interest accrued after the opening of the insolvency case and there is a prescribed rate in the Act of 8 per cent.

Payment of such interest will rank behind all other claims (except subordinated equity claims).

## Modifying creditors' rights

### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

Generally speaking unsecured claims rank *pari passu* (with some exceptions), with secured creditors afforded a level of priority by virtue of the security arrangements in place.

The court has power to change the rank of a creditor's claim in only very limited circumstances. Section 564 of the Act provides an incentive to creditors to give financial assistance or indemnities to liquidators to pursue asset recovery proceedings or to protect or preserve property. If creditors provide such assistance the liquidator may apply to the court for an order that the contributing creditors receive a higher dividend from the company's assets than they would otherwise be entitled to.

In assessing any claim under section 564, the court will consider all the circumstances surrounding the claim. Therefore, it is difficult to assess the frequency and likelihood of success attributable to any individual claim. The courts, in exercising their discretion, will have particular regard to factors such as the amount of risk to creditors, the amount recovered and the proportion between the debts of participating creditors and others, as well as the public interest in encouraging creditors to provide indemnities to enable assets to be recovered. Litigation funding can also be obtained outside the court process (see question 27).

A DOCA may determine the creditors to be paid and how much they are to be paid (noting that a level of protection is afforded to employees unless they agree otherwise). Aggrieved creditors can apply to the court to overturn a DOCA if they are discriminated against.

## Priority claims

### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Under the Act certain unsecured debts are given priority ahead of other unsecured debts. Sections 556 to 564 of the Act govern this, and the priority debts include expenses incurred by the administrator or liquidator in realising the assets of the company and in carrying on the company's business and the costs in relation to any applications to the court in respect of the winding up and employee related entitlements (discussed further below).

A company's debts to the Commonwealth government do not receive any special priority. Amounts in respect of unpaid income tax rank as unsecured debts and are payable only if there are sufficient funds left over after all preferential debts have been paid.

Certain employee entitlement claims will have priority over secured debts, which are secured by a security interest of circulating assets (ie, receivables, stock, etc).

## Employment-related liabilities in restructurings

### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Whether dismissed by a receiver or administrator or as a result of liquidation employees' wages, superannuation, leave entitlements and redundancy payments are given priority over payment of ordinary unsecured creditors in the distribution of assets in the winding up. Pursuant to the Commonwealth's Fair Entitlement Guarantee (FEG), when a company is placed into liquidation leaving employee entitlements unpaid, the Commonwealth government, through FEG, can make payments to employees of certain levels of unpaid wages, leave and other entitlements. The Commonwealth then becomes a creditor of the company and is afforded the same priority in the distribution as the employee claims it paid.

Upon the making of a winding-up order by the court, the publication of that order acts as a notice of dismissal of all employees of the company. An employee who was engaged subject to a contract of employment for a fixed term, or was entitled by his or her contract of employment to a period of notice prior to termination of the contract,

may lodge a proof of debt for damages for breach of contract. While the appointment of a voluntary liquidator does not necessarily operate as a notice of dismissal, the liquidator has the power to terminate contracts of employment.

In relation to a company in administration and receivership, upon appointment the administrator or receiver takes control of the company's business, property and affairs. The retention of employees will depend upon the outcome of the administration process. If the business is continued to be operated, then the employees are likely to be retained; however, an administrator and receiver can also terminate contract employments in the same way as management of the company could when the company was operating as a going concern.

The Act affords a level of protection to employee entitlements following the company and its creditors entering into a DOCA. The Act provides that the entitlements of employees be given certain priorities in a deed, those priorities to be at least equal to what they would receive if the company were being wound up.

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#### **Pension claims**

### **35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Employee entitlements are afforded a level of priority in liquidations, receiverships and administrations. Under section 556 of the Act employee entitlement claims are afforded a level of priority over other unsecured claims (noting that expenses of the liquidation still rank higher). It should be noted that a cap applies to the level of employee entitlements that are afforded priority for former officers of the company. In a receivership, employee entitlements are afforded priority over secured claims that are only secured by a security interest of circulating assets (the old floating charge).

A claim for unpaid employee entitlements is lodged in the same manner as other unsecured claims (ie, a proof of debt in the ordinary course). As noted in question 32, a statutory regime also exists (FEG) to supplement amounts available for employee claims.

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#### **Environmental problems and liabilities**

### **36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

Ultimate responsibility for any environmental issues will continue to rest with the relevant distressed debtor company. Upon appointment an insolvency administrator will not automatically assume responsibility for such liabilities, but will need to be aware of any such concerns and damage should they seek to continue to trade the company. Should further damage accrue during the course of the insolvency administrator trading the business, they may be held liable in the same way that directors have been held liable pre-appointment. Further, in scenarios where the insolvency administrator seeks to sell or realise the relevant asset, engagement with the environmental regulator will be required where there is pre-existing environmental damage and often remediation will be a contractual condition to the sale.

Creditors will not be held liable for controlling or remediating any environmental damage. The debtor's officers and directors could potentially be held liable for such liabilities in circumstances where the company enters formal liquidation and it can be shown the company was cash-flow insolvent at the time such liabilities were incurred. Third parties may be liable, but it will depend on the circumstances surrounding the environmental damage and any contractual obligations in place at that time.

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#### **Liabilities that survive insolvency proceedings**

### **37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

The liabilities of a corporate debtor do not subsist after a liquidation has concluded. Under either a voluntary or involuntary arrangement, the creditors will receive compensation from the company's assets in proportion to the debts owing to them in satisfaction of their claims.

The company's debts will be discharged in the context of these restructuring proceedings and thus the creditors' claims will not subsist post-winding up. As noted below, upon deregistration a company will cease to exist as a corporate entity and any surplus assets will vest in the corporate regulator.

Unsecured claims subsist after a receivership has concluded and such creditors may bring an action against the company (noting they are unlikely to do so unless significant assets remain).

The outcome of the second creditors' meeting during a voluntary administration will determine what creditors claim subsist (ie, either a DOCA or winding up is likely to commence).

Under a scheme of arrangement those creditors whose rights are not compromised or affected will continue to have their original claim against the company.

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#### **Distributions**

### **38 How and when are distributions made to creditors in liquidations and reorganisations?**

In liquidation, distribution will occur when funds are available. Under a DOCA or a scheme of arrangement, the distribution arrangements are generally set out in the terms of the respective instruments. It is possible for interim distributions to be made as funds become available.

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#### **Transactions that may be annulled**

### **39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

The following types of transaction may be held to be void and set aside after a company has entered into liquidation:

- insolvent transactions (which includes both unfair preferences and uncommercial transactions);
- unfair loans;
- unreasonable director-related transactions; and
- transactions entered into for the purpose of defeating, delaying or interfering with creditors' rights on a company's winding up.

Uncommercial transactions and unfair preferences are voidable if the company was insolvent at the time of the transaction or at a time when an act was done to give effect to the transaction. The courts have held a transaction 'uncommercial' if a reasonable person in the company's circumstances would not have entered into it. An unfair preference is one where a creditor receives more for an unsecured debt than would have been received if the creditor had to prove for it in the winding up. The other party to the transaction or preference may prevent it being held void if it can be shown that they became a party in good faith, they lacked reasonable grounds for suspecting that the company was insolvent and they provided valuable consideration or changed position in reliance on the transaction.

Loans to a company are 'unfair' and thus voidable if the interest or charges in relation to the loan were, or are, not commercially reasonable. Any 'unreasonable' payments made to a director or a close associate of a director are also voidable, regardless of whether the payment occurred when the company was insolvent.

A liquidator can seek a court order under section 588FF of the Act with respect to suspected voidable transactions. Potential orders include the repayment of money paid or retransfer to the company of property it transferred. Orders may also be made varying a contract that is part of the transaction.

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#### **Proceedings to annul transactions**

### **40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

Under Australian law, transactions will only be vulnerable to challenge when a company does in fact enter into liquidation. Only a liquidator has the ability to bring an application to the court to declare certain transactions void. In his or her report to creditors at the second meeting, a voluntary administrator may identify potentially voidable

transactions but he or she is not empowered to pursue a claim in respect of such transaction. Any such claim must be brought by a liquidator subsequently appointed.

The following transactions are voidable if they occurred within the applicable time period (transactions with related parties are afforded a longer hardening period):

- uncommercial transactions, which are voidable if entered into during or after the two years ending on the relation-back day (the relation-back day is generally the date of the application to wind up the company);
- unfair preferences, which are voidable if entered into during the six months ending on the relation-back day or between the relation-back day and the day the winding up began;
- unreasonable director-related transactions, which are voidable if entered into during the four years ending on the relation-back day or between the relation-back day and the day the winding up began;
- unfair loans, which are voidable if made any time before the winding up began; and
- insolvent transactions for the purpose of defeating creditors are voidable during the 10 years ending on the relation-back day.

Upon the finding of a voidable transaction, a court may make a number of orders, including directions that the offending person pay an amount equal to some or all of the impugned transaction; direct a person to transfer the property back to the company; or direct an individual to pay an amount equal to the benefit received.

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#### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

A director or officer of a company may be held liable under the Act for civil and criminal penalties or to compensate the company if the company incurs a debt while insolvent (otherwise known as insolvent trading). Directors and officers may also attract liability for breaching their statutory duties of reasonable care and diligence in the exercise of their powers and to act in good faith and for proper purposes. Statutory liability may also be imposed where directors or officers improperly use their position or information acquired because of their position to gain an advantage for themselves or cause detriment to the company.

In some situations directors may become personally liable for unremitted amounts of income tax or GST. The Commissioner of Taxation must give 14 days' notice to the directors setting out the details of the unpaid amount and the penalty. Directors may avoid a penalty if the company pays the unremitted amount, the company enters into an agreement relating to the unremitted amount, an administrator is appointed or the company goes into liquidation.

The courts maintain discretion under the Act to excuse directors from liability in some circumstances if they can be shown to have acted honestly and reasonably.

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#### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Cross-collateralisation and group guarantees are often sought by lenders into a corporate group. Such guarantees provide comfort that a holding company will stand behind special purpose vehicles or operating companies. There is also a statutory form of cross-guarantee lodged with ASIC allowing corporate groups to lodge consolidated financial statements. This statutory cross-guarantee provides for a group to be liable for each other group member's debts, and is designed to afford a level of comfort to creditors providing services or lending to operating subsidiaries.

Further under section 588V of the Act a holding company of a company may, in certain circumstances, be held liable for the insolvent trading of a subsidiary.

#### Pooling

As noted above at question 29 under the Act a court can make a 'pooling order' such that in the liquidation of a group of companies each of

the separate group companies are treated as if they were a single company. This means that the creditors of the group will have their claims 'pooled' so that, in effect, they are treated as creditors of one entity with a combined pool of assets for distribution.

Notwithstanding that the Act makes no provision for the pooling of assets and liabilities of a group of companies in administration, Australian courts have sanctioned the use of pooling arrangements for groups in administration proposing to execute a pooled DOCA. Ultimately this will be a decision of the creditors voting, however; a pooled DOCA will be persuasive if the return to creditors of the group as a whole will provide greater return than if the individual entities ratified separate DOCAs or were placed into liquidation.

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#### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

No. However, related party claims are likely to be subject to greater scrutiny.

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#### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

The main way in which a secured creditor may enforce its security over assets of the company outside of court proceedings is through the private appointment of a receiver as discussed above. The security agreement (ie, charge or mortgage) will normally grant the secured creditor the ability to appoint a receiver. Once appointed, the receiver will realise the company's assets solely for the benefit of the secured creditor to the exclusion of the rest of the company's creditors. A creditor may also exercise rights as mortgagee in possession and take control of the property with a view to realising value.

Retention of title clauses are another way a creditor may enforce proprietary and contractual rights outside court proceedings. If effective, this will allow the creditor to reclaim property supplied to the company in the event of the company's receivership, administration or liquidation. Retention of title clauses fall within the definition of 'security interest' under the PPSA, and are therefore required to be registered under the provisions of the PPSA. A traditional retention of title arrangement will be considered a 'PMSI' under the PPSA, and, upon registration, will give the holder priority over other registrable interests. In this sense, while the procedure for enforcing a retention of title clause will change, the effect shall remain the same.

A number of common law and statutory liens are also available (and do not require registration under the PPSA).

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#### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Deregistration can be voluntary upon the application of the company, a director, a member or a liquidator, and can be initiated by ASIC or court-ordered in circumstances where the company has no assets or liabilities or its winding up has been finalised. Upon the deregistration of the company it ceases to exist as a corporate identity.

In addition, ASIC may unilaterally deregister a corporation if it has reason to believe that the company is no longer carrying on its business, has been fully wound up, has been at least six months late in lodging its annual return or has not lodged the relevant corporate documentation (including financial reports) required by the Act in the preceding 18 months. There is, however, a process under the Act for the reinstatement of deregistered companies in certain circumstances.

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#### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

##### Voluntary administration

As described above, there are three outcomes of a voluntary administration upon which the creditors decide:

**Update and trends**

**Risks of shareholder class actions**

The emerging recognition by Australian courts of US style ‘indirect market based’ or ‘fraud on the market’ causation in shareholder class actions has caused greater uncertainty for debt-for-equity restructures, because of the increased risk of successful actions being brought. However, the risk may be addressed by the use of a provision of the Corporations Act that allows the court to approve the subordination of shareholder claims in a scheme of arrangement without the need for a meeting of shareholders to approve the scheme. The provision was relied on successfully in the *Atlas Iron* case. This makes a creditors’ scheme of arrangement an attractive option for carrying out a debt-for-equity swap in a listed entity.

**Safe harbour provisions**

The Australian government has once again foreshadowed the introduction of safe harbour provisions to shield directors from insolvent trading liabilities in certain circumstances. The proposal is still at discussion stage, with two alternatives proposed:

- a defence to the insolvent trading provisions if the director is acting on the advice of an appropriately qualified restructuring adviser; or
- a carve-out from the insolvent trading provisions if the debt was reasonably incurred for the purpose of ‘trading out’.

No draft legislation has been tabled, nor has the government proposed a timetable for doing so.

- entering into a DOCA with creditors;
- winding the company up; or
- terminating the administration.

The outcome chosen will dictate how the voluntary administration ends. Once a DOCA is executed, the company comes out of voluntary administration, and if the company terminates, the administrative control vests back in the board of directors.

**Liquidation**

At the conclusion of a liquidation the company is deregistered. The process of deregistration is regulated by Chapter 5A of the Act. After the company’s affairs are fully wound up, the liquidator must produce an account showing how the winding up has been conducted and the company’s property disposed of. The liquidator must also call a meeting of the company or, in the case of a creditors’ voluntary winding up, a meeting of the members and the creditors, for the purpose of producing and explaining the account. Within seven days of this final meeting, the liquidator must lodge a record of the minutes of this meeting and a copy of the account with ASIC. ASIC must deregister the company when three months have elapsed after the liquidator has lodged with ASIC a return stating that the final meeting has been held with a copy of the final account attached.

In a compulsory winding up, the liquidator may also apply to the court, pursuant to section 480 of the Act, for an order that the liquidator be released and that the company be deregistered after the liquidator has realised all the property of the company or so much of that property as can in his or her opinion be realised without needlessly protracting the winding up; has distributed a final dividend (if any) to the creditors, has adjusted the rights of the contributories among themselves and made a final return (if any) to the contributories. The court must be satisfied that no creditor will be adversely affected by the order.

**Receivership**

A receivership concludes when the secured assets are realised and the secured creditors are repaid (either in full or to the fullest extent possible). In such circumstances control of the company is handed back to either the directors or voluntary administrator, and in most instances the company is deregistered or wound up.

**International cases**

**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Australia formally adopted the UNCITRAL Model Law on Cross-Border Insolvency by implementing legislation called the Cross-Border Insolvency Act 2008 (Cth) (Cross-Border Act).

This legislation adopts the Model Law with as few changes as necessary to adapt it to the Australian context. Some of the most important features of the legislation include:

- the participation by foreign creditors in local insolvency proceedings;
- facilitated cooperation between courts and insolvency practitioners from different countries;
- allowing a person administering a foreign insolvency proceeding to have access to local courts and in which circumstances this is possible;
- the setting out of conditions for recognition of an insolvency proceeding and for granting relief to representatives of such a proceeding; and
- ability to effectively coordinate insolvency proceedings occurring concurrently in different states.

**Recognition and relief**

Whereas previously these issues were primarily governed by various sections of the Act, the passing of the Cross-Border Act has streamlined the regulatory framework in this area. The Cross-Border Act provides that a foreign representative (defined to include a liquidator or administrator) may apply to the court for recognition of a foreign proceeding in which the foreign representative has been appointed. ‘Foreign proceeding’ is defined to include a judicial or administrative proceeding in a foreign state pursuant to a law relating to insolvency in which managing the assets and affairs of the debtor is subject to control or supervision.

To receive recognition, evidence of the existence of the foreign proceeding must be tendered. A court has power to grant both provisional relief pending the determination of a recognition application and, if a finding of recognition is made, a broad power to grant ‘any appropriate relief’ requested by the foreign representative. The types of relief that can be granted include:

- staying the commencement or continuation of individual actions or individual proceedings concerning the debtor’s assets, rights, obligations or liabilities;
- staying execution against the debtor’s assets to the extent it has not been stayed; and
- providing for the examination of witnesses, the taking of evidence or the delivery of information concerning the debtor’s assets, affairs, rights, obligations or liabilities.

**Creditors’ rights**

Under the Cross-Border Act, foreign creditors, save for tax and penal debts, have the same rights regarding the commencement of, and participation in, insolvency proceedings as an Australian creditor. All foreign claims must be converted into Australian currency for the purposes of the proceedings.

**Recognition of foreign judgments**

As noted above, the Cross-Border Act allows for the recognition of foreign proceedings. The power to grant relief appears to extend to the enforcement of foreign judgments. Furthermore, the Foreign Judgments Act 1991 (Cth) creates a general system of registration of judgments obtained in foreign countries. This act only extends to judgments pronounced by courts in countries where, in the opinion of the governor-general, substantial reciprocity of treatment will be accorded by that country in respect of the enforcement in that country of judgments of Australian courts.

The application to register a foreign judgment must be made by a judgment creditor to the appropriate court (usually the state or

territory supreme court) within six years of the date of judgment or, if an appeal has been taken, within six years of the last judgment in the appeal proceedings.

## COMI

### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

As noted in question 47, Australia formally adopted the UNCITRAL Model Law on Cross-Border Insolvency by implementing legislation called the Cross-Border Act. Under the Cross-Border Act there is a rebuttable presumption that the centre of the debtor's main interest are its registered office, or in the case of a natural person, his or her habitual residence. The Model Laws are silent on the standard required for COMI determination.

Given this, the Australian courts have looked to and adopted similar reasoning when considering COMI as similar jurisdictions (such as the bankruptcy courts in the United States) and have equated the concept of COMI with the principle place of business. In considering where the COMI of a debtor or group of companies exists the courts will look at a number of factors, including:

- the location of the debtor's headquarters;
- the location of those who actually manage the debtor;
- the location of the debtor's primary assets;
- the location of the majority of the debtor's creditors or a majority of creditors who would be affected by the case; and
- the jurisdiction whose law applies to most disputes.

## Cross-border cooperation

### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Section 581 of the Act provides that an Australian court may request a foreign court with jurisdiction in external administration matters to render assistance in the recovery of overseas property of the company. In deciding whether to authorise a letter of request, one important consideration will be how likely it is that the foreign court will act upon the request.

The Cross-Border Act provides an alternative method whereby an Australian insolvency practitioner may seek recognition under the Model Law in a foreign jurisdiction and thereby give the foreign court independent jurisdiction to provide assistance. Under the UNCITRAL Model Law, the insolvency practitioner may then have authority to recover assets in the foreign jurisdiction.

In relation to insolvency proceedings conducted in a foreign jurisdiction, section 581 of the Act also provides that an Australian court must assist bankruptcy courts of prescribed countries and has a discretion to assist courts of other countries. The prescribed countries are Jersey, Canada, Malaysia, Papua New Guinea, New Zealand, Singapore, Switzerland, the United Kingdom and the United States. Once again, the Model Law provides an alternative procedure, whereby a representative in a foreign jurisdiction may approach an Australian court requesting assistance in the recovery of property located in Australia belonging to the foreign company. In *Re Cow Cho Poon (Private) Limited* (2011) 249 FLR 315 a Singaporean liquidator made application to an Australian court pursuant to section 581 of the Corporations Act seeking declarations that he was authorised to open, close, redesignate and operate certain bank accounts held by the company in Australia. In granting the relief sought the Australian court noted that to so order would be of utility and would aid the effectuation of the winding-up orders made by the Singapore court. It is likely that a similar result would have been reached had the Model Law been invoked.

While in most cases Australian courts have formally recognised foreign proceedings under section 581 of the Act when requested to do so, there have been exceptions. For example, in the recent case of *Yu v STX Pan Ocean Co Ltd (South Korea), in the matter of STX Pan Ocean Co Ltd (receivers appointed in South Korea)* [2013] FCA 680 the court was reluctant to grant additional relief as the relief sought would adversely affect any rights that other Australian creditors may otherwise have had, whether under the Act or otherwise.

There are no reported cases of an Australian court refusing to recognise foreign proceedings or grant relief sought under the Cross-Border Act in relation to a corporate insolvency.

## Cross-border insolvency protocols and joint court hearings

### 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

Many of the cases involving cross-border elements heard in Australian courts involve the protection of assets and the issuance of injunctions or stay orders. One such example was the case of *Lawrence v Northern Crest Investments Limited (in liq)* [2011] FCA 672, where an interim injunction was granted against the Australian directors of an insolvent New Zealand company restraining them from dealing with the company's assets, pending an application by the liquidator for orders that the winding-up proceedings in New Zealand be classified as a 'foreign main proceeding'.

There have been no joint hearings or formal arrangements made to coordinate proceedings with courts in other countries to date.



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# Austria

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

Insolvency proceedings, which include bankruptcy proceedings, reorganisation proceedings with self-administration and reorganisation proceedings without self-administration, are governed by the Austrian Insolvency Code (the Insolvency Code).

In addition to the Insolvency Code, the Business Reorganisation Law of 1997 (the Business Reorganisation Law) governs a specific form of 'reorganisation' supporting the restructuring of a solvent debtor's business. 'Reorganisations' under the Business Reorganisation Law are not insolvency proceedings and do not affect creditors' rights.

An Austrian debtor is deemed to be insolvent when it is either illiquid or (in the case of corporate entities) over-indebted.

According to case law, a debtor is illiquid when it lacks the means to pay all of its liabilities that are currently due. Liabilities due in the future (even if they are already known) are not taken into consideration for this test. The inability to satisfy liabilities when due constitutes illiquidity only if it is permanent rather than merely temporary (as a result of any cash-flow restrictions).

According to case law, a debtor is over-indebted if the assets (based on their liquidation value) would not be sufficient to satisfy all of its creditors and a business forecast shows that the debtor is likely to become illiquid (ie, unable to pay its debts) in the future and, as a result thereof, will be liquidated. The first limb of the test is objective and will be satisfied if a debtor's liabilities exceed the value of its realisable assets. It assumes an orderly voluntary liquidation of assets on the valuation date rather than valuing the company as a going concern. The second limb of the test requires an analysis of the probability that the company will become illiquid within a reasonably predictable period (usually at least the current and the following fiscal year).

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Insolvency proceedings are generally conducted by the competent provincial court (in Vienna, the Commercial Court) in the area where the debtor's business is located; failing this, for example when the debtor is a private person, by the court of the place where the debtor has its permanent residence, its branch office or any assets. In the case of a natural person applying for insolvency proceedings, the competent district court is involved.

There are no special restrictions on the matters the courts may deal with, provided that the conditions required for the instigation of the insolvency proceedings are met (see question 9).

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

In general, both individuals and legal entities, including general partnerships, limited partnerships, professional partnerships, professional

limited partnerships and European economic interest groupings as well as a deceased person's estate, can be subject to insolvency proceedings. The Supreme Court has ruled that even municipalities may be subject to insolvency proceedings.

Owing to a lack of legal standing, civil partnerships, silent partnerships and cartels cannot enter into insolvency proceedings. Only their partners may be subject to insolvency proceedings.

Reorganisation proceedings with or without self-administration and reorganisations under the Business Reorganisation Law do not apply to credit institutions, insurance companies and pension funds. For such entities, special provisions set out in the Banking Act, the Insurance Company Supervision Act and the Pension Fund Act apply. The Business Reorganisation Law also does not apply to investment service companies, financial institutions and leasing companies.

The following assets are excluded from insolvency proceedings and are exempt from claims of creditors: inheritances, legacies and gifts to the extent not accepted by the insolvency administrator; any assets that the insolvency court decides to release from the estate; claims arising in the context of legal proceedings asserted by the debtor and assets in the possession of the debtor the restitution of which is subject to legal proceedings to the extent the insolvency administrator does not enter into such proceedings; all rights that are incapable of being transferred to a person other than the debtor; and, when the debtor is a natural person, a certain amount of monetary funds that is granted to the debtor for his or her living expenses.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Investments of the Republic of Austria in partially or entirely nationalised companies are in most cases administered via the Austrian State and Industrial Holding Company (ÖBIB), an Austrian limited liability company which holds the shares in these companies. The ÖBIB is the successor of the former Austrian State Industrial Holding Stock Corporation (ÖIAG), which has been turned into ÖBIB in early 2015 by way of a form-changing transformation pursuant to the Austrian Stock Corporation Act.

Other shareholdings in government-owned enterprises (eg, the Federal Railways Company) are directly held by the Republic of Austria and administered by the government.

Since all these nationalised companies and government-owned enterprises are set up under Austrian private law (most often in the form of a limited liability company or a stock corporation), there are no specific procedures as to the insolvency of these enterprises. Consequently, the creditors' remedies are also the same as in ordinary insolvency proceedings.

Statutory bodies under public law (eg, municipalities, cities with their own charter, federal states and the Republic of Austria itself) may also become insolvent. This is generally accepted and derived from their general legal capacity. Therefore in principle, in the case of an insolvency of a statutory body with general legal capacity, the Austrian Insolvency Code will apply.

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**Protection for large financial institutions**


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**5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered ‘too big to fail’?**

In July 2013 Austria adopted a resolution regarding the intervention in and restructuring of financial institutions (BIRG) in order to stabilise the Austrian financial market and avoid the need to allocate public funds for credit institutions facing financial difficulties. According to BIRG, institutions must provide the Austrian financial authority (FMA) with reorganisation and liquidation plans in advance in order to put the FMA in a position to take reasonable steps should a trigger event (being specific circumstances defined by the financial institutions as events exceeding the risk bearing ability of the financial institutions) occur. A crisis affecting the entire Austrian financial market should be preventable as reorganisation of the financial institution should be possible without public funding and liquidations taking place without any unexpected economic consequences. No institution is (legally) qualified as ‘too big to fail’, but the principle of proportionality applies, whereas an exemption for smaller institutions without relevance to the Austrian financial market as a whole can be made. However, the FMA is not allowed to waive the requirement of drawing up a reorganisation and liquidation plan when the financial institution has subsidiaries in another member state of the EU or another state; the total balance sheet of the institution or the group exceeds €5 billion; or the ratio between the total balance sheet of the institution or the group and the Austrian gross domestic product exceeds 3 per cent.

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**Secured lending and credit (immoveables)**


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**6 What principal types of security are taken on immoveable (real) property?**

The two principal types of security available for immoveable property are mortgages and the transfer of title in property. In a mortgage, the debtor remains the owner. In a transfer of title in property, the transferee is registered as the owner but merely holds the property as a trustee for the transferor.

Both types of security are valid only when registered with the Land Registry. The priority of one of several mortgages on the same piece of immoveable property usually depends on the chronological order of the entry into the Land Registry.

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**Secured lending and credit (moveables)**


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**7 What principal types of security are taken on moveable (personal) property?**

The principal types of security available for moveable property are pledges and transfers of title for the purpose of taking security. The most common is the assignment of receivables as a security device. However, for such assignments and pledges to be effective as regards third parties, strict publicity requirements must be complied with. For example, for receivables, by notification of the assignment to the third-party debtor or alternatively, by appropriate notes in the assignor’s accounts from which it is readily ascertainable when and in whose favour the assignment was made. The priority of a pledge or assignment depends on the time the publicity requirement was met.

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**Unsecured credit**


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**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

As long as no insolvency proceedings have been opened, unsecured creditors may enforce their claims (court judgments, enforceable notarial deeds, etc) according to the provisions of the Austrian Enforcement Code. In these proceedings, an unsecured creditor may, among others, apply for the compulsory creation of a mortgage over the debtor’s real property. Normally, however, enforcement would be directed against the property, receivables, rights and any other assets of the debtor.

Procedures under the Enforcement Code are usually time-consuming, in particular if they involve the forced administration or forced sale of real property.

In principle, no special procedures apply to foreign creditors as such, provided they hold a valid Austrian claim for enforcement. However,

special procedures apply with regard to foreign titles. Recognition and enforcement of such foreign titles in enforcement proceedings are regulated by bilateral and multilateral treaties between Austria and the country in which the title was issued. Austria is a party to the Lugano Convention, and is subject to the Brussels Convention on jurisdiction and the enforcement of judgments in civil and commercial matters of 1968, the Council Regulation (EC) No. 44/2001 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters and the Brussels Regulation (EU) No. 1215/2012 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (recast).

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**Voluntary liquidations**


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**9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?**

Under Austrian law, the term ‘voluntary liquidation’ of a company is used to refer to a company being dissolved by its shareholders voluntarily according to its corporate charter outside the scope of insolvency proceedings. In such a case, all creditors’ debts must be fully satisfied before the liquidation can be completed.

The following does not deal with ‘voluntary liquidation’ in the strict Austrian sense of the word but with the true situation when the directors of a company (as opposed to its creditors) can, and are under certain circumstances required to, file for insolvency proceedings. A debtor is required to initiate a voluntary liquidation if the insolvency test is met (see question 1). Therefore, the debtor is required to apply for the opening of insolvency proceedings if it is illiquid or – if the debtor is a legal entity – if it is over-indebted, that is, if liabilities exceed assets based on liquidation values (ie, there is negative equity). However, according to settled case law, the fact that a legal entity has negative equity triggers an obligation to apply for insolvency only if the company is not a going concern.

Following the application for opening insolvency proceedings, the court examines the application and decides whether the debtor meets the insolvency test. If this is the case, the court will open insolvency proceedings immediately.

Once the court has formally opened insolvency proceedings (with the exception of reorganisation proceedings with self-administration), the right to make any dispositions with respect to the insolvency estate and the administration thereof passes from the debtor to the insolvency administrator appointed by the court. In such case, only the insolvency administrator is entitled to act on behalf of the insolvent’s estate. Transactions concluded by the debtor after the opening of insolvency proceedings are void with respect to the creditors. If the court makes an order for reorganisation proceedings with self-administration, the debtor retains the right to make dispositions with respect to the insolvency estate, but will be supervised by a court-appointed reorganisation administrator.

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**Involuntary liquidations**


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**10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

Each (individual) creditor may also apply for the opening of insolvency proceedings with respect to a debtor. The creditor will need to establish that the debtor is insolvent (ie, either illiquid or over-indebted without a going concern prognosis, although, realistically, a creditor will usually only be able to demonstrate the former) and that he has a valid claim against the debtor, even if this claim is not yet due for payment. If the court is satisfied that the insolvency test is met the court will open insolvency proceedings without undue delay after the creditor has made its application. The effects of the commencement of the insolvency proceedings – where there are sufficient funds available to bear the costs of the insolvency proceedings – are the same as described in question 9.

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**Voluntary reorganisations**


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**11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

If the conditions for the opening of insolvency proceedings are met (see question 1) or there is a real threat of the debtor’s inability to pay debts as they fall due (‘pending illiquidity’), the debtor may apply to

court for the opening of reorganisation proceedings. A reorganisation proceeding can only bind unsecured creditors (and secured creditors to the extent that their claim is under-secured). The debtor may also apply for the opening of reorganisation proceedings after insolvency proceedings have been opened as long as such proceedings have not been concluded. An application for the opening of reorganisation proceedings must include a reorganisation plan offering payment of at least 20 per cent of the claims to unsecured creditors within two years of the approval of the reorganisation plan. The court will appoint a reorganisation administrator who is in charge of the company until the reorganisation plan is approved. The approval of the reorganisation plan requires a majority of (unsecured) creditors holding more than 50 per cent of the aggregate claims of those (unsecured) creditors present at the relevant court hearing.

Alternatively, the debtor can apply for reorganisation proceedings with self-administration. In such a case, the reorganisation plan has to provide an offer for the payment of at least 30 per cent of the (unsecured) creditor's claims within two years after approval. An inventory of assets, a current status report as well as a liquidity plan for the following 90 days has to be provided at the time of application. The advantage of reorganisation proceedings with self-administration is that the debtor does not lose control over the assets to an insolvency administrator, allowing the debtor to retain control over its business and, also, the proceedings themselves. Only for legal acts that are not considered to be in the ordinary course of business is the reorganisation administrator's approval required. Note that only an insolvency administrator can take avoidance actions, hence these are not available in a reorganisation. If the reorganisation plan is not approved within 90 days from the beginning of the proceedings, the self-administration will be revoked and an insolvency administrator will be appointed. During the continuation of the proceedings under the insolvency administrator, the reorganisation plan itself can still be approved by the creditors.

The approval of the reorganisation plan results in the conclusion of the insolvency proceedings and the withdrawal of the insolvency administrator. Furthermore, the debtor is relieved of the obligations towards its creditors exceeding the quota offered in the reorganisation plan; creditors can only set off their claims in accordance with the quota of the reorganisation plan whereas before the approval, it is possible to set off the entire claim (provided general requirements are met (see question 17)).

A debtor who is neither insolvent nor over-indebted may also apply to the court for the opening of reorganisation proceedings under the Business Reorganisation Law. If certain financial ratios are not met, application for reorganisation is mandatory. The application should include a reorganisation plan, which may be supplied up to 60 days after the filing of the application. The court will appoint a reorganisation auditor to examine and assess the reorganisation plan. As already mentioned, the opening of reorganisation proceedings under Business Reorganisation Law will not change the situation of creditors as this reorganisation is not an insolvency proceeding.

### **Involuntary reorganisations**

#### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

Only the debtor may file an application for the commencement of reorganisation proceedings. Creditors may only apply for the initiation of insolvency proceedings with respect to a debtor (see question 10).

### **Mandatory commencement of insolvency proceedings**

#### **13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

Managing directors of a company must file for insolvency without undue delay, but in any case within the first 60 days of the company becoming illiquid or over-indebted within the definition of the Insolvency Code (see question 1). During the 60-day period, the managing directors may make reasonable efforts to restructure the company or may prepare an application for reorganisation proceedings. The managing directors will be personally liable for the damage

inflicted on the company's creditors by their failure to make a timely application for the opening of insolvency proceedings, as set out below.

As regards existing creditors, the managing directors will be liable for a reduction in the insolvency quota. As regards new creditors, the managing directors will be liable for the damage suffered by such new creditors having placed confidence in the company being solvent. In addition, managing directors will be liable to the company for any payments that it has made to any counterparties while the company was insolvent. It is generally accepted that this does not apply where insolvency proceedings are diligently prepared and where the payment is necessary to protect the position of the company's general creditors.

Other than civil liability, criminal liability may also arise out of crimes such as fraud, disloyalty or specific actions such as the fraudulent preference of a creditor or the fraudulent infringement of the insolvency law.

### **Doing business in reorganisations**

#### **14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

Only during reorganisation proceedings with self-administration may a debtor carry on business (see question 11). In reorganisation proceedings with self-administration, the debtor is not required to surrender control of its entire assets to an insolvency administrator. Nevertheless, a court-appointed reorganisation administrator has a right of veto over any ordinary transactions of the debtor and must expressly agree to all transactions of the debtor beyond the ordinary course of business, as well as specific decisions, as set out in the Insolvency Code. The sale of assets is subject to the reorganisation administrator's approval to the extent that such a sale does not fall within the scope of the debtor's ordinary course of business and may be subject to the approval of the creditors' committee and the insolvency court if the sale is of the debtor's assets. With regard to mutual contracts not yet fulfilled by either party, the debtor may choose either to rescind such contracts or to have them fulfilled by both sides (subject to approval by the reorganisation administrator).

In order to facilitate the continuation of the debtor's business, termination rights in contracts with the debtor may be limited. If termination of a contract with the debtor could put the continuation of the debtor's business at risk, the contractual partners may, for a period of six months after the opening of the insolvency proceedings, terminate contracts concluded with the debtor only for 'good cause'. 'Ordinary termination' without good cause (for instance, at mutually agreed periods or dates) is prohibited. Furthermore, the deterioration of the debtor's economic situation and a payment default of the debtor in relation to obligations due prior to the initiation of the insolvency proceedings do not constitute 'good cause' for termination. However, the restrictions do not apply if the cancellation of a contract is essential for avoiding severe personal or economic disadvantages for the counterparty.

Further, termination rights based solely on the initiation of insolvency proceedings are invalid. Only certain financial and derivative contracts, which are usually entered into under master agreements that provide for the mutual set-off of claims ('close-out netting') are exempt from this rule.

The creditors must file their claims against the debtor in court. The court may appoint a creditors' committee to supervise the acts of the insolvency or reorganisation administrator. Apart from that, all the creditors meet only once, at the reorganisation hearing where the creditors vote on the reorganisation plan. The main duties of the court are to hold the opening hearing and the reorganisation hearing as well as issuing the necessary decisions.

In reorganisation proceedings under the Business Reorganisation Law, the conditions for the debtor to carry on business are as described in question 11. In essence, the court opens business reorganisation proceedings, appoints and supervises the reorganisation auditor and closes reorganisation proceedings. The creditors do not have any special rights to supervise the debtor's business activities. Indeed, they are not affected by the reorganisation at all. However, certain bridge loans

(and similar measures) granted in the reorganisation are, under certain circumstances, protected from avoidance if the reorganisation is not successful and insolvency proceedings are opened.

#### Stays of proceedings and moratoria

##### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

After the opening of such reorganisation proceedings, legal disputes with regard to the insolvent's assets may no longer be filed against the debtor and pending lawsuits concerning the debtor's assets will be suspended. Any court order rendered after the opening of insolvency proceedings will be void. Generally, all claims against the debtor must be filed with the insolvency court and examined by the insolvency administrator before litigation proceedings may be continued. Where a creditor had his claim rejected in the examination hearing, he may initiate proceedings against the debtor.

If the court has ordered a stay of the proceedings, the insolvency administrator is entitled to continue the proceedings.

In business reorganisation proceedings under the Business Reorganisation Law, pending court proceedings are not affected.

#### Post-filing credit

##### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Once insolvency proceedings have been formally opened by the court, the administration of the insolvent's assets is exclusively conferred upon an insolvency administrator. The insolvency administrator is, in principle, entitled to conclude credit agreements on behalf of the estate.

In reorganisation proceedings with self-administration, the debtor is not fully deprived of its ability to enter into transactions with respect to its assets (see question 11). The debtor is, however, prohibited from concluding certain transactions, such as selling real estate or granting sureties. Entering into loans (whether secured or unsecured) is not specifically prohibited. Nevertheless, the debtor must obtain the approval of the reorganisation administrator for any transaction beyond the ordinary course of business. Borrowings might therefore need such approval, depending on the ordinary course of the specific business.

In reorganisation proceedings under the Business Reorganisation Law, no specific limitations on post-filing credit apply.

#### Set-off and netting

##### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Generally, creditors are entitled to exercise their rights of set-off and netting in pending insolvency proceedings provided that the claims to be compensated were mutual at the time of the opening of insolvency proceedings. A creditor may not, however, set-off a claim that arose within the last six months before the formal opening of insolvency proceedings if the creditor knew, or should have known, of the debtor's illiquidity. Importantly, as opposed to the general rules of civil law, claims that have not become due at the time of the opening of insolvency proceedings, as well as claims that are subject to a condition, may be set off in the insolvency. Special netting rules apply under the Financial Collateral Act.

In reorganisation proceedings under the Business Reorganisation Law, the situation of the creditors is not affected. Therefore, no special rules on set-off apply.

#### Sale of assets

##### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

#### Insolvency

In insolvency proceedings, the sale (or lease-out) of specific immovable assets is subject to the prior approval of the court and the creditors' committee, and must be publicly announced at least 14 days (in urgent cases, eight days) in advance. The same applies to the sale (or lease-out) of the debtor's entire business (or the debtor's controlling share in a business), the debtor's entire moveable assets (whether fixed assets or current assets) and assets that are necessary for the debtor's operations. The insolvency administrator must hear the debtor with respect to these transactions before he decides to take any action. Generally, assets are sold by the insolvency administrator in a private out of court sale. A court sale will occur only if determined by the court at the insolvency administrator's application. Thus it would be permissible for the insolvency administrator to negotiate an interim sale agreement with one party while continuing to seek better bids. However, Austrian law prohibits credit bidding in a sale of the insolvent's assets – a creditor only has a claim for receipt of the insolvency quota in insolvency proceedings (principle of equality between creditors). A court would therefore have no discretion to assess a credit bid. Similarly, the credit bid of an assignee of the original secured creditor would not be permitted either.

Provisions of Austrian law related to the transfer of liabilities upon the purchase of a business do not apply if the seller of such a business is insolvent. These provisions relate to general liabilities of the seller as well as social security, other pension liabilities and liabilities relating to public charges and taxes. Lease contracts that are filed with the commercial register pass over automatically, but employment contracts do not.

Specific assets may be affected by certain encumbrances and will possibly not be transferred clear of such encumbrances. Such encumbrances may, however, lapse upon bona fide acquisition of ownership of the relevant assets.

#### Reorganisations

In reorganisations (both with and without self-administration), all transactions (including asset sales) outside the debtor's ordinary business, as well as any sale of real estate, the granting of a lien over any asset, the granting of sureties, as well as transactions without due consideration, are subject to the reorganisation administrator's prior consent. All other transactions may be vetoed by the reorganisation administrator. In reorganisation proceedings, it would be permissible for the insolvency administrator to negotiate an interim sale agreement with one party while continuing to seek better bids. Credit bidding in a sale of the insolvent's assets would also be permissible as part of the reorganisation plan, provided that the special majority and quorum requirements are met. As credit bidding would result in the unequal treatment of creditors (the credit bidder is privileged), in addition to the general majority and quorum requirements set out in question 23, such reorganisation plan would have to be approved by the majority of the disadvantaged insolvency creditors who are entitled to vote and present at the voting hearing with the total claims of the consenting creditors amounting to at least 75 per cent of the claims of the disadvantaged insolvency creditors present at the voting hearing. Apart from that, no further specific assessment concerning the credit bid would be necessary. As Austrian insolvency law states that in the case of an assignment the legal standing of the debtor may be neither improved nor deteriorated, the same must apply to an assignee of the original secured creditor. However, if the assignee has acquired the claim after the opening of insolvency proceedings, he will be deprived of his voting rights unless he was obliged to acquire the claim because of an agreement set up before the opening of the insolvency proceedings (this rule applies to insolvency and reorganisation proceedings alike).

Concerning the transfer of liabilities with certain assets, the same rules apply as in insolvency proceedings, except that employment contracts are transferred to the purchaser of an entire business.

### Intellectual property assets in insolvencies

**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

The licensor or the owner of the IP right has, by operation of law, no right to terminate a contract with the debtor simply because insolvency proceedings are opened over the debtor's assets.

In insolvency proceedings the insolvency administrator has the right to terminate any commercial contract not yet completed in full at the time the insolvency proceedings are opened. If the contract is terminated, the counterparty may claim damages in the insolvency proceedings as an ordinary unsecured creditor. However, the insolvency administrator, on behalf of the debtor, may elect to adopt the contract, in which case the contract remains in force and the contractual obligations of both parties remain intact and have to be fulfilled in full.

The court may set a deadline for the insolvency administrator to declare whether he or she wishes to adopt the contract. Such deadline must not be set earlier than 93 days after the opening of insolvency proceedings. If the debtor is defaulting on a non-monetary obligation, the period for the insolvency administrator to declare his or her position is not more than five working days after the application for declaration by the insolvency administrator by a creditor.

### Personal data in insolvencies

**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Data processing activities during insolvency proceedings are governed by the Austrian data privacy regulation as set out in the Austrian Data Protection Act (DSG).

Thus, the debtor's obligation to disclose any necessary information to the insolvency administrator must not infringe the data subject's right to the protection of personal data. Further, the insolvency administrator is required to safeguard the interests of the relevant data subjects (eg, the debtor's employees or customers). In general, as long as the debtor has lawfully processed the data to be disclosed, the disclosure of non-sensitive data can be justified by the overriding legitimate interest pursued by the controller or by a third party, whereas the disclosure of sensitive data (ie, data relating to a natural person's race, political opinion, trade-union membership, religion, health or sex life) can only be justified by the data subject's explicit consent.

Transfer of personal data to a purchaser is also subject to the provisions set out in the DSG. If the purchase of debtor's personal data is conducted via an asset deal (ie, a third party acquires some or all of the operating entity's assets containing personal data), the transfer of such data can only be justified as set out above, that is the transfer of non-sensitive data may be justified by overriding legitimate interests and for transferring sensitive data individual explicit consent from the affected data subjects has to be obtained prior to such transfer. Where the personal data collected by the debtor are purchased via a share deal (ie, the purchaser acquires the shares of the (insolvent) operating entity from the entity's shareholder or shareholders), the DSG does not restrict the transfer of sensitive and/or non-sensitive data to the purchaser.

### Rejection and disclaimer of contracts in reorganisations

**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

The insolvency administrator has the right to terminate any contract that has not been fulfilled at the time of opening of the insolvency proceedings (see question 19).

In a reorganisation, the debtor can terminate employment or lease contracts but only with the consent of the reorganisation administrator. Further, employment contracts may only be terminated in relation to employees that work in such parts of the business that will either be closed or reduced in size or, if the continuation of the business was not published in the insolvency register, after four months of the reorganisation proceedings opening. The reorganisation administrator may only give his or her consent to a termination if the fulfilment of the relevant contract jeopardises the conclusion or fulfilment of the reorganisation plan or jeopardises the continuation of the debtor's business. The employee or tenant can claim damages arising from the termination of the respective contract. Such claims are subject to the reorganisation and will be settled only with the quota set out in the reorganisation plan.

When the insolvency administrator decides to adopt a contract, he or she must comply with its obligations thereunder. Obligations arising under such contract (and with respect to breaches thereof) after the opening of insolvency proceedings lead to a preferential claim of the third party against the debtor or the debtor's estate.

### Arbitration processes in insolvency cases

**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Generally, arbitration procedures are rarely used in insolvency proceedings. In insolvency proceedings, the insolvency administrators are generally not bound by any arbitration agreements entered into by the debtor, except for the circumstances described in the following paragraphs. The insolvency court has sole and exclusive jurisdiction to hear the subject matter of the insolvency case. Any prior arbitration agreement between the debtor and its creditors with respect to the conduct and subject matter of insolvency proceedings would be void. As a consequence, an arbitration proceeding would only take place in cases where the administrator agrees to a (renewed) arbitration agreement after the initiation of the insolvency proceedings.

Based on the avoidance rules set out in the Insolvency Code, if insolvency proceedings are opened, the insolvency administrator has the right to challenge the validity of certain business transactions concluded by the debtor prior to the opening of insolvency proceedings. The debtor cannot validly enter into an arbitration agreement with respect to such proceedings prior to the opening of insolvency proceedings; additionally the insolvency administrator would not be bound by such an agreement because the avoidance claims arise only after the opening of insolvency proceedings and for the benefit of the insolvent's estate. The debtor cannot legally dispose of such claims. However, the insolvency administrator may enter into arbitration proceedings on its own account with respect to avoidance claims, but this possibility is very rarely used.

Where the insolvency administrator has adopted a contract (see questions 19 and 21), he is bound by the contractual provisions and any arbitration agreement contained therein.

Apart from contractual proceedings, an insolvency administrator is typically engaged in court proceedings with respect to some of the creditors' own property that was commingled with the insolvent's estate, or with respect to the realisation of security relating to some creditors' secured claims. Legal scholars hold the view that in these cases, the insolvency court has no exclusive jurisdiction to hear such proceedings. Consequently, the insolvency administrator remains

bound by any arbitration agreement concluded between the debtor and its creditors or third parties and the court will allow any pending arbitration proceedings to continue.

Except for the aforementioned prohibitions, disputes can be arbitrated with the consent of the parties and the insolvency administrator after the insolvency case has been opened. The court has no right to direct the parties to submit any disputes to arbitration. It should be noted that the solvent claimant would usually have to pay the costs of arbitration in advance for itself as well as the insolvent respondent.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

Mandatory features of a reorganisation plan include full satisfaction of all secured and preferential claims, as well as the debtor's offer to pay to all unsecured creditors at least 20 per cent of the outstanding claims within two years after the approval of the reorganisation plan. In the case of reorganisation proceedings with self-administration, the debtor has to offer the payment of a quota of at least 30 per cent (as well as satisfaction in full of all secured and preferential claims).

Secured creditors are creditors holding a secured right over the assets of the debtor (lien, mortgage, etc). Preferential claims include the costs of the reorganisation proceedings, various disbursements of operating costs and expenses (for instance, claims of employees for normal salary accruing after the opening of the reorganisation procedure) and remuneration for certain creditors' associations as defined by law.

The reorganisation plan must be approved by unsecured and non-preferential creditors representing more than 50 per cent in value of the total outstanding unsecured, non-preferential debts, as well as the (simple) majority of the creditors (by headcount) that are present at the reorganisation hearing.

Generally, the reorganisation plan must treat all unsecured and non-preferential creditors equally. Deviations from this principle are possible if the reorganisation plan is approved by the majority of the unsecured creditors present at the reorganisation hearing (by headcount) and creditors representing at least 75 per cent of the outstanding unsecured non-preferential debt.

The Insolvency Code does not foresee the possibility that a reorganisation plan includes releases in favour of third parties.

In business reorganisation proceedings under the Business Reorganisation Law, the reorganisation plan must include an analysis of the reasons for the need to reorganise, the necessary measures envisaged, the chances of success, the amount of additional credit needed and a timetable. The reorganisation auditor has to agree on the restructuring plan and the court has to approve this. The creditors have no right of objection.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

Reorganisations may be 'pre-packaged' or structured within certain limits. This may be the case if the offered settlement does not meet the minimum targets (notably, the satisfaction quota) imposed by law (see question 23) and therefore one or several large creditors need to subordinate their claims for the reorganisation to be approved by the court.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

If the reorganisation plan does not secure the necessary majority and quorum of the creditors' vote during the reorganisation hearing, it fails. Furthermore, the court can, and in some circumstances has a duty to, reject a reorganisation plan even though that it has been approved by the creditors (eg, if material regulations have not been complied with, or if the reorganisation plan favours certain creditors). If the reorganisation plan is not approved, the reorganisation proceedings are continued as bankruptcy proceedings.

The approved reorganisation plan may be actively monitored by a reorganisation administrator if agreed upon in the reorganisation plan. During such supervision the court may issue protective measures with regard to the debtor's assets and may veto certain legal transactions. If a debtor defaults on its payment to a particular creditor, the creditor has to notify the debtor of this and grant it a two-week grace period. If the debtor is still unable to fulfil its obligations after such period, the original claim of this creditor is re-established in its totality, (ie, not only in the reorganisation quota). Despite a default with respect to a particular creditor, the reorganisation plan and the quota remains in effect with respect to those creditors on whom the debtor has not defaulted.

If a reorganisation plan under the Business Reorganisation Law is not approved by the court, reorganisation proceedings must be closed.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The decision on the opening of insolvency proceedings, as well as other decisions issued by the court, must be published. As of 1 January 2000, all notices of decisions of the court are published on a special website ([www.edikte.justiz.gv.at](http://www.edikte.justiz.gv.at)) for a limited period.

The court holds several public hearings during insolvency proceedings, the most important being the general creditors' meeting immediately after the opening of the proceedings; the examination hearing, at which the insolvency administrator acknowledges or rejects the claims filed by the creditors; and the reporting hearing at which the insolvency administrator submits a report on the status of the proceedings. Other meetings can be held at the court's discretion or mandatorily, if such a meeting is demanded by the insolvency administrator, the creditors' committee or at least two creditors representing claims of at least one-quarter of the total claims – secured as well as unsecured – against the debtor. All meetings are called by the court and published on the internet.

In the reporting hearing the insolvency administrator reports on the prerequisites for the closing of the business or parts of the business or the continuation thereof, as well as on any reorganisation plan and the viability thereof.

The insolvency administrator has to give a statement of accounts at the end of the insolvency proceedings and whenever the court issues instructions to do so.

No creditor may initiate proceedings on behalf of the debtor to pursue remedies (such as avoidance proceedings) against third parties during insolvency proceedings. Only the insolvency administrator is entitled to do so. However, each member of the creditors' committee may file an application with the court to have the insolvency administrator removed from office. Additionally, the court may at any time remove the insolvency administrator at its own initiative.

Upon final confirmation of the reorganisation plan, the debtor is released from its liabilities in accordance with the reorganisation plan. However, a reorganisation plan may not provide for the release of liabilities owed by third parties. Therefore, while the debtor may also be released from its liabilities towards jointly liable parties (eg, guarantors), all such jointly liable parties will remain liable to the debtor's creditors.

If the debtor is in default of its payment obligations under the reorganisation plan, the original liabilities may be reinstated, provided that the creditor has given due and timely notice of the default. In principle, the liabilities are reinstated proportionally (ie, if 75 per cent of the insolvency quota has already been paid, 25 per cent of the original liability will be reinstated). Thus, provided that the quota pertaining to a certain liability has been paid in its entirety according to the reorganisation plan, such original liability will not be reinstated. In general, the reorganisation plan may not deviate from this provision to the detriment of the debtors. If the whole reorganisation plan is annulled, different rules will apply.

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**Enforcement of estate's rights**


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**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

Generally, if the insolvency court determines that the available assets are insufficient even to cover the costs of instituting insolvency proceedings, it will dismiss the application for the opening of insolvency proceedings for lack of funds. If a claim is available to the estate and the court determines that this claim is worth pursuing, but the estate lacks adequate funds to do so, it may oblige the creditor that filed the application for the opening of insolvency proceedings to advance funds to enable the insolvency administrator to pursue the claim. It should be noted that managing directors of legal entities and shareholders holding more than 50 per cent of such legal entity's shares can be held liable to pay a proportion of the anticipated costs to cover the insolvency proceedings. Where insolvency proceedings are not initiated because of a lack of funds, neither the debtor nor the creditors would benefit from the effects of insolvency proceedings.

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**Creditor representation**


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**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

The creditors' committee, consisting of three to seven members, is appointed by the court on its own initiative or upon application by the creditors, if the particular features of the case indicate that the establishment of a creditors' committee is necessary. In practice, a creditors' committee is established in all large-scale insolvency cases. The appointment has to be based on proposals by the creditors, representatives of the debtor's employees and other special interest groups.

The creditors' committee has to supervise and support the appointed insolvency administrator and approve the sale or the lease of the debtor's business and all of the debtor's moveable or immovable assets. Furthermore, the creditors' committee has to audit the cash administered by the insolvency administrator.

Members of the creditors' committee may not claim any remuneration beyond the compensation of their expenses, such as travelling expenses and necessary costs of experts.

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**Insolvency of corporate groups**


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**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

Under Austrian insolvency law, insolvency proceedings against a parent and its subsidiary may only be combined for procedural purposes and must be heard by the same judge. The proceedings themselves remain independent of one another and the assets and liabilities are not combined into one pool for distribution purposes.

According to article 35 of the EC Council Regulation (EC) 1346/2000 on Insolvency Proceedings any assets remaining in Austria shall be transferred to an administrator outside of Austria only if it is possible to meet all claims in Austria by the liquidation of assets in Austrian secondary proceedings. Other than such transfer of surplus assets, Austrian law does not provide a mechanism to transfer assets subject to insolvency proceedings in Austria to an administration in another country.

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**Appeals**


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**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

Austrian law distinguishes between three types of court orders: those that can be appealed with an autonomous recourse, those that can only be appealed together with another appealable decision and those that

cannot be appealed at all. The remedy against court orders is always a 'recourse'. The general rules according to the Civil Procedures Act apply.

The requirements for bringing a recourse are:

- damage ('formal damage', meaning that the court's decision differs from the party's motion, is sufficient);
- legitimacy (every party to the proceedings);
- timeliness (14 days, starting from the day of delivery of the court order);
- no waiver or withdrawal of the appeal;
- form; and
- content (declaration of appeal, reason for appeal and claim).

In insolvency matters, the appellant is allowed to bring new facts or evidence during recourse proceedings, provided that they already existed at the time when the appealed decision was made.

Recourses do not have a delaying effect on the enforceability of the court order. However, the court cannot alter the appealed decision to the detriment of the appellant, which means that as a worst-case scenario for the appellant, his or her recourse gets rejected.

If the requirements of a recourse are met, the appellant is entitled to bring an appeal. As a prerequisite to the decision of the appellate court, the trial court, where the appeal was submitted, decides on the admission of the appeal. After admission, the appeal is submitted to the appellate court, which also has the right to reject the recourse.

Defendants can require non-EU applicants to post security for court fees except where the applicant has its usual place of residence in Austria, a court order for compensation would be enforceable in the applicant's usual place of residence, in marital disputes, in disputes relating to bills of exchange or when the plaintiff has sufficient real estate (secured) assets.

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**Claims**


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**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

After the opening of insolvency proceedings, creditors have to submit a notification of their claims to the court. The deadline for filing creditors' claims is established by the court in its order to open insolvency proceedings. Claims may also be filed after the deadline but such claims will not upset preceding distributions to the creditors and creditors who filed late will not have the right to appeal other claims, which have been filed in time.

The insolvency administrator accepts or rejects the notified claim at the examination hearing and any creditor may dispute the validity or priority of the claim. Confirmation of a claim by the insolvency administrator has a binding effect with respect to its amount but not as to whether such claim is a preferential claim or an unsecured claim. Creditors whose claims are rejected by the insolvency administrator or denied by the other creditors (ie, those with contested claims) may bring an application for the court's confirmation that their claims are valid.

Contingent claims may be notified to the court with their complete (maximum) amounts. In the event of suspensive conditions (ie, where the claim arises only after the condition has been met), the quota relating to such contingent claim will be secured by the court and paid to the creditor only after the relevant condition has in fact been met. In the event of resolute conditions (ie, where an existing claim is extinguished when the condition has been met), the quota relating to such claim may either be secured by the court or ordinarily paid to the creditor, provided that in exchange the creditor provides security to the court in the event that the resolute condition is met and the claim is extinguished thereafter and the creditor has to pay back the quota.

Unliquidated claims may also be notified to the court. The notification has to provide an estimate by the creditor of the claim's value as at the opening of the insolvency proceedings. The estimate may be challenged by the administrator and, as a result, the court decides upon the value of the claim by appointing expert witnesses.

There are no specific provisions in the Insolvency Code governing the transfer of claims. The transfer is restricted only because the claim will have been deemed to be acquired after the opening of insolvency proceedings. This results in the transferee not being able to set off the transferred claim against any other claims of the debtor against the transferee existing before such opening of insolvency proceedings. There is no legal obligation to notify the insolvency administrator of the transfer.

Claims acquired at a discount can still be enforced for their full face value. However, a party is not entitled to set off an obligation it has regarding the insolvency estate with a claim it has acquired after the initiation of insolvency proceedings (and under certain circumstances when the third party knew or ought to have known of the insolvency of the common debtor, even before the initiation of insolvency proceedings).

Interest accruing from the date of the opening of an insolvency proceedings cannot be claimed as an insolvency claim during the proceedings. However, the opening of reorganisation proceedings does not stop interest from accruing unless the parties agree on a discharge of residual debt during the course of such proceedings.

### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

In general, Austrian insolvency law is based on the principle that in insolvency proceedings, all creditors rank equally. However, secured creditors enjoy priority to the extent of their security rights. Preferential creditors also enjoy priority (see question 33). Also, claims of creditors whose claims arose after the opening of insolvency proceedings rank above other claims.

Only if the insolvency administrator challenges the claim of a particular creditor may the court decide that the creditor's claim is, in fact, different in nature from that alleged by the creditor and may assign it to a different class, thereby also changing its priority. However, this happens infrequently and the question in most cases is whether the security of a secured creditor is valid.

### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

In essence, preferential claims are the costs of the insolvency proceedings, the disbursement of expenses for the insolvency estate's maintenance and management, certain early termination claims (see question 19), claims for fulfilment of mutual contracts (provided that the insolvency administrator has adopted such contracts) and the remuneration of certain creditors' associations that participate in the proceedings. Claims accrued prior to the opening of the proceedings (including taxes, social security contributions, wages and salaries) are not privileged.

Secured creditors' claims are not affected by the insolvency. However, if the enforcement of such rights threatens the continuation of the insolvent's business, satisfaction of such claims may be postponed for a period of six months after the beginning of the insolvency proceedings. Post-opening claims are not satisfied from valid security rights of a creditor (with the exception of costs having arisen specifically with respect to the disposal of the security).

### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

The employee's ordinary wages accrued prior to the opening of insolvency proceedings are deemed to be insolvency claims; ordinary wages accrued after the opening of insolvency proceedings are privileged and will be satisfied prior to the insolvency claims of unsecured creditors.

In insolvency proceedings the administrator has a privileged right to terminate employment contracts in relation to employees that work in such parts of the business that will either be shut down or reduced in size or, if the continuation of the business was not published in the

insolvency register, during the fourth month after the opening of the reorganisation proceedings. When the termination of an employee's contract is based on the administrator's privileged right, the termination compensation of the employee, according to Austrian employment law (eg, holiday compensation, severance compensation and other damages), is deemed to be an unsecured claim. If the termination of an employee's contract does not fulfil the preconditions of the aforementioned right of the administrator, the termination compensation will be satisfied prior to the insolvency claims of unsecured creditors.

Austrian law does not provide for any insolvency-specific claims arising out of the termination of employment contracts and any specific procedures with regard to such terminations.

### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Austrian employers can make contributions to a statutory pension either by a defined benefit to the employee, making direct payments, or by making contributions to a pension fund for the benefit of the employee.

Claims by retired employees already having a right to receive defined benefit payments from the employer should be handled in the same way as ordinary employee wages. Therefore deficiencies accrued prior to the opening of insolvency proceedings are deemed to be unsecured claims, whereas deficiencies accrued after the opening of insolvency proceedings are privileged and will be satisfied prior to the insolvency claims of unsecured creditors. On the other hand, claims of the retired employee against pension funds are not affected by the employer's insolvency.

Most prospective entitlements of employees are subject to the Austrian Company Pensions Act (BPG). These claims should also be treated in the same way as ordinary wages, as described above. If the employment contract is terminated before or because of the insolvency proceedings, claims in this respect form part of the termination compensation and are deemed to be unsecured claims. Termination of the employment for any other reason leads to these claims being privileged claims and therefore satisfied with priority to unsecured insolvency claims.

Prospective entitlements falling beyond the scope of the BPG are treated as being subject to a suspensive condition (the employee's retirement) and, therefore, the quota relating to such contingent claim will be secured by the court and paid to the creditor only after the relevant condition has in fact been met. In any case a certain percentage, depending on the individual circumstances, of the employer's pension-related claims will be covered by a fund established solely for the benefit of employees in the event of the employer's insolvency under Austrian law. Employees' claims against pension funds are not affected by the employer's insolvency.

### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

After the initiation of insolvency proceedings, public regulations, including environmental regulations, continue to be relevant for the affected parties.

The debtor's obligation to take all necessary measures regarding environmental requirements persists. Since the insolvency administrator takes over all duties related to the insolvency estate, the administrator also represents the debtor in dealing with the authorities, including with respect to environmental matters.

Where the relevant requirements are not met, the public authority may initiate substitute performance. Costs arising as a result thereof after the initiation of insolvency proceedings are preferential costs and are therefore incurred to the detriment of the general insolvency creditors.

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**Liabilities that survive insolvency proceedings**


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**37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

If insolvency proceedings are terminated, the creditors would again have the right to pursue all their claims against the debtor without limitation. Any funds received by them during the insolvency proceedings would be taken into account. However, if the debtor is a commercial entity and the insolvency proceedings lead to a liquidation of the debtor, the debtor would be deleted from the commercial register and cease to exist after the termination of the insolvency proceedings (unless assets of the debtor emerge, in which case the debtor would be deemed to continue in existence).

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**Distributions**


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**38 How and when are distributions made to creditors in liquidations and reorganisations?**

Distributions may only be made after the general examination hearing has been held. The final distribution may only take place after all assets have been sold, all decisions have been issued by the courts on contested creditors' claims, the insolvency administrator's fees have been determined and the final accounts of the insolvency administrator have been approved by the court. This can only be done on the basis of a draft distribution document and a distribution hearing.

In reorganisation proceedings, payments must be made in accordance with the approved settlement plan.

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**Transactions that may be annulled**


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**39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Only the insolvency administrator is entitled to challenge transactions undertaken by the debtor prior to the opening of insolvency proceedings (covering liquidations as well as reorganisations) during the respective 'suspect period'. In this respect, the Insolvency Code provides for various cases of avoidance on a number of grounds and with different suspect periods. The decision lies within the insolvency court. For example, transactions in which the debtor intentionally put certain creditors at a disadvantage relative to one or several other creditors who knew of such an intention result in a suspect period starting 10 years before the opening of insolvency proceedings. In other cases, suspect periods range between six months and two years. Such cases include the transfer of assets without due consideration (two years), provision of security or settlement of an obligation not due at such time (one year), and business transactions with the insolvent debtor when the counterparty knew or should have known of the insolvency (six months). The provisions, and settled case law regarding them, are complicated and sometimes make it difficult to predict whether a particular transaction may become subject to avoidance in a future insolvency.

If the avoidance motion is successful, the transaction will be declared as being without any effect as regards the other creditors.

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**Proceedings to annul transactions**


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**40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

The Insolvency Code recognises the concept of a 'suspect period' to determine whether a transaction of the debtor may be challenged (see question 39). Depending on the grounds for challenging the transaction, the 'suspect period' is between six months and 10 years. Only the insolvency administrator may challenge a transaction. A transaction would be declared void as regards the creditors in the case of a successful challenge. The grounds for voidability are as follows:

- (i) intentionally putting assets beyond creditors' reach: bad intent applies only if the transferor or chargor acted with the intent to create a disadvantage for its creditors and if such intent were known or deemed to be known by the other party;

- (ii) squandering applies only if the transferor or chargor's actions within the last year preceding the opening of insolvency proceedings were seen as squandering of assets and if such squandering were known or deemed to be known by the other party;
- (iii) if the transaction was undertaken by the debtor for no consideration or deemed to be for no consideration within the past two years preceding the initiation of insolvency proceedings; and
- (iv) if the transaction unduly favours a certain creditor and pertains to legal acts of the debtor having taken place within the last 60 days preceding insolvency or after an application to open insolvency proceedings, or when the debtor was (materially) insolvent.

The transaction unduly favours a certain creditor if:

- such creditor acquires a security or satisfaction to which kind, or at which time such creditor is not entitled to such security or satisfaction;
- the security or satisfaction takes place for the benefit of close relatives if the respective intent to unduly favour these creditors is known or deemed to be known by them; or
- the security or satisfaction takes place for the benefit of others and such people know or are deemed to know of the intent of the common debtor to disadvantage its creditors.

Voidance under the foregoing is excluded if the undue favouring of certain creditors took place more than one year preceding the initiation of insolvency proceedings.

A transaction of the debtor may be void if it took place after insolvency or after the application to open insolvency proceedings on the grounds of knowledge concerning the common debtor's insolvency in the following circumstances:

- with regard to close relatives of the covenant debtor; or
- if a creditor acquires security or satisfaction or if a legal transaction entered into by the debtor puts the creditors at a disadvantage. If the transaction resulted in an indirect disadvantage, it may be challenged only if the disadvantage was 'objectively foreseeable' for the other party. In particular this is the case if (at the time of the transaction) it had been obvious that a restructuring concept was not feasible.

Voidance under the foregoing is excluded if the respective legal acts took place more than six months prior to the initiation of insolvency proceedings.

Outside of the insolvency proceedings, creditors may challenge transactions under the Voidance Act in the circumstances described in (i) and (iii) above only.

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**Directors and officers**


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**41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

The managing directors of a company are liable to the company for any failure to perform their function in a diligent manner. Any resulting claims the company has against the directors are subject to a five-year limitation. The company may not waive or agree to settle these claims to the extent that payment by the managing directors is required to satisfy the company's creditors. Directors may also be liable directly to creditors if they failed to file for insolvency (see question 13). Also, the Tax Procedure Act and social security legislation impose personal liability on managing directors to the extent that they have failed to diligently manage funds available to the company, where such funds should have been paid on account of taxes or similar circumstances. Under Austrian social security legislation, a managing director may even be subject to criminal liability for having failed to make pro rata social security contributions on any salary payments that were subject to such contributions.

Under the Business Reorganisation Act, managing directors are personally liable for the company's debt up to €100,000 per individual, if they failed to instigate the opening of business reorganisation proceedings upon having received a report by the company's auditor stating that the company was in need of reorganisation. This is the case if the company's equity ratio is less than 8 per cent, and the implied debt settlement period exceeds 15 years, unless an opinion is issued

by a certified auditor confirming that there is no need for reorganisation. The liability arises if, within two years of the managing directors receiving the auditor's report, insolvency is applied for. In certain circumstances, members of the supervisory board or shareholders of a limited liability company may also become liable under the Business Reorganisation Act.

In specific circumstances, the managing directors could also be liable under the Austrian Criminal Act for offences such as fraudulent conveyance or intentional preference of a creditor in the state of insolvency. While other employees may also become liable to the company, that liability is limited under the Employee Liability Act.

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### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

In general, the assets of parent (and also affiliated) corporations have to be separated from the assets of subsidiaries (and affiliates) (principle of separation). Therefore, parents or affiliated corporations can only be held responsible for the liabilities of subsidiaries or affiliates if they have contractually agreed to be liable. However, certain circumstances can arise under which shareholders can be held directly liable, although this is highly controversial in legal literature and little case law exists. The following situations could give rise to direct responsibility of parent or affiliated corporations:

- mingling of assets: if the assets of the parent or affiliate cannot be clearly separated from the assets of the subsidiary or affiliate (ie, because of lack of accounting);
- qualified material undercapitalisation: if the subsidiary or affiliate has been provided with little equity, imposing a higher risk of creditors not being satisfied than in the ordinary course of business; however, intentional dealing would be required from the parent or affiliate to be held liable in this respect;
- factual management of the shareholder: if the shareholder conducts the subsidiary's or affiliate's business in a way the managing director would normally do;
- infringement of the subsidiary's or affiliate's assets leading to illiquidity: if the shareholder treats the assets of the company in a way that leads to loss of the subsidiary's or affiliate's liquid funds; and
- infringement of a legal nature: if the shareholder abuses the legal structure of the subsidiary or affiliate in order to minimise liabilities.

Moreover, Austrian capital maintenance rules may also give rise to claims of subsidiaries or affiliates against their parents or affiliated corporations if they breach the foregoing rules.

Austrian corporate law prohibits the return of equity from a company to its shareholder. A company may not make any payments to shareholders other than the distribution of profit or during the course of a formal reduction of statutory capital. Provisions on the repayment of capital also cover benefits granted by the company to its shareholders where no 'adequate consideration' is received in return. Such consideration must, as a minimum standard, be no lower than a comparable consideration that the company would have received from an unrelated third party. Any agreement between a company and its shareholder or any third party granting an advantage to the shareholder that would not, or not in the same way, have been granted for the benefit of an unrelated third party is void and any profit received has to be returned. In insolvency proceedings, the insolvency administrator can enforce this claim against the parent or affiliated corporation. In the case of an Austrian stock corporation, claims can be enforced directly by the creditors of the subsidiary or affiliate.

Under the Austrian law on equity substitution, loans from shareholders to companies suffering a 'crisis' (when applying for insolvency proceedings or 'reorganisations' under the Business Reorganisation Law) are classified as substitutions of equity and are therefore treated differently. According to the Insolvency Code, shareholders' claims in this respect are subordinated and can only be satisfied after satisfaction of all unsecured and preferential claims and only if the insolvency court agrees to accept these claims in the course of the insolvency proceedings. Shareholder loans granted outside of a 'crisis' rank *pari passu* with other senior claims.

Austrian case law has clearly stated that with respect to group companies considered one economic entity, the principle of legal separation must be respected regardless of economic considerations. This

applies not only for the purpose of general corporate law, but also specifically with respect to insolvency law. Moreover, it was reiterated that in insolvency proceedings there can be only one debtor – the individual company whose assets must be considered individually. Thus, the transfer of assets between several insolvent debtors is prohibited and a court cannot order the distribution of company assets among these, even if they are companies within the same group.

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### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

In this respect, annulment of transactions as described in question 39 should be taken into consideration, since any provision of security or settlement of an obligation towards the parent or affiliated company not due at such time (60 days before the opening of the insolvency proceedings) could be challenged by the insolvency administrator and payments made to these 'insiders' clawed back. See also question 42 in respect of subordination of shareholder loans if made in times of crisis.

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### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Out-of-court enforcement over the debtor's assets is possible if these assets have been provided to a creditor as security and out-of-court enforcement has been agreed in the agreement for the provision of such security.

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### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

General company law provides for standard procedures for dissolving a corporation (called 'voluntary liquidation' under Austrian law; see question 9). Such procedures are quite different from insolvency proceedings and do not require the court to become involved, apart from removing the business from the commercial register. In a voluntary liquidation, all creditors must be fully satisfied.

A corporation is already dissolved by operation of mandatory Austrian law upon the opening of insolvency proceedings. In place of the corporation, its assets form the insolvent's estate, which is sold off and the proceeds are eventually distributed to the creditors.

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### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Insolvency cases are concluded by a formal order of the insolvency or reorganisation court after all conditions for the closing of the procedure have been fulfilled.

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### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

The Insolvency Code includes rules on cross-border insolvency proceedings. The newly adopted provisions apply insofar as no international treaty or the EC Council Regulation (EC) 1346/2000 on Insolvency Proceedings is applicable. Most importantly, assets located outside Austria may become the subjects of insolvency proceedings in Austria. Further, Austrian courts will recognise and enforce foreign insolvency proceedings insofar as the standards of the foreign insolvency proceeding are comparable to Austrian insolvency proceedings

and provided that the debtor's main centre of interests is located in the foreign jurisdiction. Generally, according to newly introduced conflict-of-laws provisions, the laws of the place where the insolvency proceedings are initiated govern the entire proceedings. Special conflict-of-laws provisions apply in certain situations or matters (eg, real property). These principles also apply to reorganisation proceedings.

By the same amendment, Directives 2001/17/EC on the reorganisation and winding-up of insurance undertakings, and 2001/24/EC on the reorganisation and winding-up of credit institutions, were implemented in Austria.

Austria is also subject to the EC Regulation on Insolvency Proceedings replacing existing bilateral insolvency treaties. For further information see the chapter on the European Union.

Generally, foreign creditors are treated on an equal footing with Austrian creditors during insolvency proceedings taking place in Austria, and are free to file the same applications and notifications of claims as Austrian creditors. However, they must appoint a person residing in Austria who is empowered to accept service on behalf of the foreign debtor.

The UNCITRAL Model Law on Cross-Border Insolvency is under consideration in Austria. There are ongoing working sessions of the 'special task force for insolvency law' of the Ministry of Justice.

## COMI

### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

The definition of COMI emerges from European Union Law. There is a general presumption that the COMI of a corporate debtor is at its registered office. See further the chapter on the European Union. Austrian courts focus on objective criteria and therefore the COMI should be ascertainable by third parties. This presumption can be rebutted whenever there are signs indicating that the main administration is in another country. In the case of a group insolvency, the COMI of each subsidiary has to be determined individually.

## Cross-border cooperation

### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

The Insolvency Code allows for cross-border cooperation in several ways. The Austrian insolvency court and the Austrian administrator have to provide to the foreign administrator any information deemed to be of importance for conducting the foreign insolvency proceedings without undue delay. Furthermore, the foreign administrator shall be granted an opportunity to submit its own proposals relating to the liquidation or the utilisation of assets located in Austria or to submit statements in relation to reorganisation plans.

In addition, in the case of recognition of foreign insolvency proceedings, the foreign administrator may also exercise the powers granted to it by local laws in Austria except with regard to coercive actions and decisions over legal or other disputes.

The Austrian Supreme Court has not yet dealt with a case where a lower court has refused to recognise foreign proceedings or to cooperate with foreign courts.

According to the Insolvency Code, the effects of foreign insolvency proceedings are recognised if the debtor's centre of main interests lies within a foreign country and the basic principles of these proceedings are similar to those in Austria, in particular the treatment of Austrian and foreign debtors (see question 47).

Within the European Union any insolvency proceedings are recognised in other member states as soon as the opening of the proceedings are in effect (see the chapter on the European Union).

We are not aware of a case where recognition has been refused.

## Cross-border insolvency protocols and joint court hearings

### 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

We are not aware of any such protocols or hearings. There is no basis for these in Austrian law as currently in force.



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# Bahamas

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Bahamas has recently undergone a major reform of its company liquidation regime. The Companies (Winding up Amendment) Act and the International Business Companies (Winding up Amendment) Act were enacted during April 2012 as part of a suite of reform initiatives to modernise our commercial legislation. The reform saw the introduction of new Rules (the Companies Liquidation Rules 2012) applicable to all companies, which came into force on the 31 July 2012. Under the new regime, the meaning of insolvency has been expanded beyond the traditional 'cash-flow test' to include the 'balance sheet test'. As such a company is insolvent not only if it is unable to pay its debts as they fall due, but also if the value of the company's liabilities exceeds its assets.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The Supreme Court has exclusive jurisdiction over corporate insolvencies, from presentation of a winding-up petition to conclusion of the process. This is so for both ordinary companies and IBCs. There are practically no restrictions on the jurisdiction of the court as it relates to insolvencies. The Supreme Court may make winding-up orders in respect of 'an existing company', a company incorporated and registered under the Companies Act or the IBC Act, a body incorporated under any other law, and (now under the new regime) a foreign company that has property located in the Bahamas, is carrying on business in the Bahamas or is registered in the Bahamas.

Appeals against decisions and orders of the Supreme Court lie to the Bahamas Court of Appeal and, ultimately, to the Judicial Committee of Her Majesty's Privy Council, which sits in London, England.

Actions merely seeking the repayment of debts or damages of B\$5,000 or less are heard in the magistrates (lower) court.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

No entities are expressly excluded from the application of the general statutory provisions governing corporate insolvencies. However, there are modifications in their application with respect to, for instance:

- insurance companies, which require the Insurance Commission to be a party to proceedings for winding-up and which may in certain circumstances be wound up on the application of policyholders;
- banks, which may be wound up on the application of the governor of the Central Bank for the purposes of protecting depositors and others; and
- investment funds, which must notify the Securities Commission in writing of the commencement of any winding-up, dissolution or other termination procedures.

Similarly, generally all assets of a company are subject to the winding-up process. This is obviously without prejudice to and after taking into account and giving effect to the rights of preferred (ie, taxes, employee entitlements, etc) and secured creditors. Indeed notwithstanding that a winding-up order has been made, a creditor who has security over assets of a company is entitled to enforce his or her security without the leave of the court and without reference to the liquidator. Similarly, property held on trust by a company, although subject to control of the liquidator, will not be available for general distribution. There is now, however, under the new regime, recovery of liquidator's costs in relation to assets held upon a trust. Assets available to satisfy creditors are now not burdened by such costs as they are borne by the persons who benefit from the trust asset.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Government-owned enterprises (or corporations) in the Bahamas are governed by individual statutes that usually establish such enterprises as body corporates with perpetual succession and a common seal and with power to acquire, hold and dispose of property, to enter into contracts, to sue and be sued in its own name and to do all things necessary for their established purposes. As such, the insolvency procedure followed for such enterprises are the same as has now been introduced under the Companies Liquidation Rules 2012 (as herein discussed), which are applicable to all companies. The remedies that creditors of insolvent public enterprises have are therefore the same as creditors of any other private company (see questions 7 and 8).

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

The legal mortgage constitutes the principal form of security taken over real property. This involves the transfer of the whole of the mortgagor's legal interest in the property to the mortgagee, subject to the mortgagor's right to redeem legal title upon repayment of the debt (known as the 'equity of redemption').

An equitable mortgage may also be taken over immovable property. Unlike a legal mortgage, this involves no transfer of any legal estate or interest to the creditor but rather confers an equitable interest in the land. The holder is entitled to have the property subject to the mortgage sold by order of the court to realise the security.

The fixed charge is another form of security frequently taken over immovable property in the Bahamas. Under this arrangement the asset in question (whether currently owned by the debtor or not) is charged with the satisfaction of the debt immediately upon the debtor acquiring an interest in it.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

Various forms of security are taken on personal property. The form used is largely dependent upon the nature of the asset in question, the interest of the debtor therein and the objectives of the creditor in taking the security.

Mortgages and charges are frequently taken over specific assets such as ships, aircraft, vehicles and shares. Hypothecations of cash deposits are regularly used by lenders seeking protection against default on loan obligations, especially where overdraft facilities have been provided. Legal assignments of choses in action are also commonplace in the lending context, particularly as it relates to receivables and insurance policy proceeds. Debentures (incorporating both fixed and floating charges) are widely utilised as a security instrument over both specific assets and assets that may be changed from time to time, such as stock in trade, book debts, office equipment, furniture and raw materials.

There are no statutory formalities contained in the Companies Act or the IBC Act governing the creation of security interests generally. Under the IBC Act, however, a charge of shares of an IBC must indicate an intention to create a charge and indicate the amount secured by the charge or how that amount is to be calculated. A charge of shares of an IBC may also be governed by the law of a jurisdiction other than the Bahamas.

The question whether an instrument has been effective to create a floating charge or a fixed charge is determined according to principles derived from English common law and will be based on:

- the terms of the security document;
- the nature of the rights created in favour of the charge-holder and those retained by the debtor; and
- the nature of the property being encumbered.

Liens essentially confer a legal right to retain possession of goods until money owed to the holder has been paid. They may arise by contract, statute or operation of law. This form of security commonly arises locally in favour of specific office holders, professionals and tradesmen who provide labour or incur expenses for which they are entitled to be remunerated. These include provisional liquidators, receivers and receiver managers, attorneys and workmen who expend labour and skill on improving or repairing chattels bailed to them.

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## Unsecured credit

### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

An unsecured creditor generally has no special rights over the property and assets of a debtor until he or she obtains and enforces a judgment. Where there are concerns that assets belonging to the debtor may be dissipated or removed from the jurisdiction prior to judgment being given, the creditor may obtain *Mareva* injunctive relief to restrict dealings with the assets in question or other assets potentially capable of satisfying any judgment. This will often require the giving of an undertaking to repay the debtor for any financial losses suffered by reason of the restrictions imposed should the unsecured creditor's claim ultimately fail.

A range of enforcement procedures are available to an unsecured creditor who has obtained a judgment in his or her favour. These include:

- writs for the seizure and sale of the debtor's goods and assets;
- garnishee orders attaching money due to the judgment debtor by third parties;
- charging orders;
- receivership; and
- orders for committal.

The procedure to be invoked is primarily influenced by the amount of the debt owed and the nature of the goods available to satisfy the judgment.

Under the Rules of the Supreme Court, the court has the discretion to require a creditor who is not ordinarily resident within the jurisdiction to pay 'security for costs' as a precondition to pursuing legal proceedings in the Bahamas. The factors taken into consideration in making such an order normally include the estimated future legal costs of the defendant in resisting the proceedings, the legal costs already incurred by the defendant, whether the claimant has any property or assets within the jurisdiction and the overall merits of the substantive claim. The sum required will not normally provide a defendant with a full indemnity in respect of his or her likely legal costs, but it will make some funds available from which a defendant may recoup costs in the event that he or she successfully defends any legal proceedings pursued against him or her.

A straightforward debt collection action may be completed within a few months of the initial filing of the claim. The time taken to dispose of such claims usually depends on the complexity of the matter and the extent to which the debtor resists the proceedings.

Under the Reciprocal Enforcement of Judgments Act, judgments and arbitrators' awards from jurisdictions that accord similar recognition to Bahamian Supreme Court judgments may be registered and thereafter enforced locally. The preconditions to obtaining registration include:

- application to register must generally be made within 12 months from the date of the judgment;
- the foreign court must have acted with jurisdiction;
- the judgment must not have been obtained by fraud; and
- recognition of the foreign judgment must not be against public policy.

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## Voluntary liquidations

### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A company may commence voluntary liquidation in the following situations:

- a period fixed for its duration by the articles of association expires or a specific event occurs after which it is to be dissolved under its articles;
- a resolution requiring the company to be wound up voluntarily has been passed by at least 75 per cent of its members; or
- if the company resolves by resolution that it be wound up voluntarily because it is insolvent.

Indeed, a voluntary winding-up is deemed to commence:

- at the time of the passing of the resolution for winding up; or
- on the expiry of the period or the occurrence of the event specified in the company's memorandum or articles, notwithstanding that a supervision order may be subsequently made by the court.

After commencing voluntary liquidation, the company must cease to carry on business except as required for its beneficial winding up, although the company's articles, its corporate state and powers continue until the company is dissolved. If the winding up has commenced in accordance with the occurrence of an event in the memorandum and articles of the company, then the person designated therein shall become liquidator (known as 'voluntary liquidator') automatically from the commencement of the winding up. If no such person is designated (or such designated person is unable or unwilling to act) then the directors shall convene a general meeting of the company for the purpose of appointing a liquidator. In this latter scenario, the appointment only takes effect upon the filing with the Registrar of the nominated liquidator's consent to so act. On the appointment of a voluntary liquidator all the powers of the directors cease, except so far as the company in a general meeting or the liquidator sanctions their continuance.

Within seven days of the commencement of the voluntary liquidation, the voluntary liquidator, or in his or her absence, the directors shall:

- file with the Registrar of Companies a notice of the winding up;
- file with the Registrar of Companies the voluntary liquidator's consent to act;
- in the case of a regulated company, send a copy of documents referred above to the regulator; and
- publish a notice of the voluntary winding up in the gazette.

A very important requirement for a voluntary liquidation is that within 35 days of the commencement of a voluntary liquidation, the voluntary

liquidator shall file with the Registrar of Companies, a director's declaration of solvency, duly signed by all directors. Indeed in the absence of such a declaration, the voluntary liquidator must make an application to the court for a supervision order and must give notice of such application to the registrar.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

A creditor (by assignment or otherwise) is entitled to petition the Supreme Court for an order that a company be wound up on the basis of its inability to pay its debts or on grounds that it is just and equitable to do so. A company may be deemed to be unable to pay its debts in the present context where:

- it is indebted in a sum exceeding B\$1,000 and, after being served at its registered office with a demand requiring payment of the sum due, it has failed to do so for at least three weeks;
- enforcement of a judgment or order in favour of the creditor against the company is returned unsatisfied in whole or in part;
- it can be proved that the company is unable to pay its debts (this raises balance sheet considerations); or
- it can be proved that the value of the company's assets is less than the amount of its liabilities, having regard to its contingent and prospective liabilities (this raises liquidity considerations).

Prior to the first appointment of liquidators, the court may appoint a provisional liquidator to take charge of the estate and effects of the company pending the hearing of the petition. All dispositions of property, transfers of shares and alterations in the status of members of the company between commencement of winding up and the order for winding up are void unless otherwise approved by the court.

Once a winding-up order has been made or a provisional liquidator has been appointed, no actions or proceedings against the company may be instituted or continued without the permission of the court. After winding up, the management powers of the directors come to an end and are exercisable by the liquidators.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The Bahamas does not currently have comprehensive statutory procedures addressing financial reorganisations of insolvent companies. Reorganisations of IBCs are addressed in the IBC Act under the heading Merger, Consolidations etc. Under the Act, the directors of a company may, by a resolution of directors, approve a plan of arrangement. 'Arrangement' is defined as:

- a reorganisation or reconstruction of a company;
- a separation of two or more businesses carried on by a company; or
- any combination of any of the things specified above.

Upon approval of the plan of arrangement by the directors, the company shall make application to the court for approval of the proposed arrangement. The court may determine what notice, if any of the proposed arrangement is to be given to any person; determine whether approval of the proposed arrangement by any person should be obtained and the manner of obtaining the approval; determine whether any holder of shares, debt obligations or other securities in the company may dissent from the proposed arrangement and receive payment of the fair value of his or her shares, debt obligations or other securities. The court may also conduct a hearing and permit any interested persons to appear; and may approve or reject the plan of arrangement as proposed or with such amendments as it may direct.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

There are at present no procedures in either the Companies Act or the IBC Act expressly entitling a creditor to commence an involuntary reorganisation of an insolvent company.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

There is no express obligation under Bahamian law requiring a company's board to commence insolvency proceedings. Directors are nonetheless under statutory duties to the company to act in good faith and with a view to its best interests, and to act with reasonable prudence in the discharge of their functions. They may also potentially be subject to criminal or civil sanctions for certain types of misconduct and omissions. Where winding up is clearly warranted and would be in the best interests of the company, a company's board would therefore be at risk in continuing to trade as normal.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

A liquidator may carry on the business of the company so far as is necessary for its beneficial winding up. The extent to which this power is exercisable will depend upon the terms of the liquidator's appointment. Outside of the insolvency context, the conditions and extent to which a company may carry on business during reorganisation will depend on the terms of the plan of arrangement approved by the court.

A company about to be wound up voluntarily may by resolution delegate to its creditors or to a committee of creditors the power of appointing liquidators or filling vacancies in the office of liquidator. It may also enter into similar arrangements concerning the powers to be exercised by liquidators and the manner of their exercise.

Under the Insurance Act 2005 the Supreme Court has the power to place a company that carries on insurance business under 'judicial management' instead of ordering it to be wound up. The application for such an order is made by the industry regulator (ie, the Insurance Commission) and is appropriate, for example, where winding up may have far-reaching negative consequences for policyholders or the general public. The judicial manager in such situations may be empowered to continue to carry on business with a view to its reorganisation even though the company may be technically insolvent. He or she would, however, be subject to court control in the performance of his or her duties at all times.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

The making of an order for winding-up by the court or the appointment of a provisional liquidator triggers an automatic stay of all suits, actions and other proceedings against the company, both under the Companies Act and the IBC Act. The automatic stay is wide in scope and would apply to creditors' actions.

The continuation of any legal proceedings or the commencement of a new action in such circumstances may only be undertaken with the permission of the court. A creditor would accordingly have to make application to the court to commence or continue proceedings after winding up. Conditions may also be imposed on the grant of such permission.

There is no automatic stay of suits, actions and proceedings in a voluntary winding up as there is in a compulsory winding up. Application would therefore have to be made to the court to restrain such claims.

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**Post-filing credit**
**16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

A liquidator appointed under both the Companies Act and the IBC Act may, with approval from the court:

- carry on the business of the company, so far as may be necessary for its beneficial winding up;
- raise money on the security of the company's assets;
- draw, make and indorse promissory notes on behalf of the company; and
- do and execute all such other things as may be necessary for winding up the affairs of the company and distributing its assets.

Secured or unsecured loans or credit may thus be obtained for the beneficial winding up of a company, notwithstanding that it is in liquidation. No special priority is at present accorded to such loans over existing secured lenders whose rights are already fixed. Such loans would, however, rank ahead of ordinary unsecured creditors.

Financial reorganisation is a voluntary process initiated by resolution of a company's board, frequently where insolvency is not in issue. A debtor involved in this process may obtain secured or unsecured loans or credit provided this is not prohibited under the plan of arrangement governing the reorganisation. Unless special terms have been agreed under the plan, the normal rules as to priorities under the general law would apply to loans or credit obtained.

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**Set-off and netting**
**17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

Any contractual right of set-off or non set-off or netting arrangement agreed between the company and any creditor prior to the commencement of the liquidation (including both bilateral and multilateral set-off or netting arrangements) are binding upon the company in liquidation and shall be enforced by the official liquidator.

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**Sale of assets**
**18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

The conditions attaching to the sale of assets during a reorganisation depends largely on the terms of the plan of arrangement approved by the court and the articles of arrangement governing the process. Dispositions of assets comprising more than 50 per cent in value of the assets of the company not done in the ordinary course of business must be approved by directors and members, with notice in prescribed terms being given of any members' meeting to address the issue.

The sale of assets during liquidations (voluntary or involuntary) is addressed in statute. Unless otherwise ordered, in a compulsory liquidation a liquidator is required under the Companies Act and IBC Act to obtain the prior approval of the court before selling the real or personal property or effects of the company, including choses in action. In a voluntary winding up the liquidator may dispose of assets without approval of the court. The extent to which a liquidator in a court-supervised winding up may make such dispositions depends on the restrictions imposed upon him or her in the exercise of his or her functions by the court.

A purchaser generally acquires the assets 'free and clear' of any claim or interest. If the assets themselves (eg, land or chattels) are subject to third-party interests, the new owner may end up taking subject to these.

'Stalking horse' bids and credit bidding by secured lenders are not expressly addressed in the Bahamian insolvency statutes. Any adoption of these procedures would have to meet the approval of the court.

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**Intellectual property assets in insolvencies**
**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

An IP licensor possesses no express statutory power to terminate a debtor's right to use intellectual property once insolvency proceedings are commenced. His or her ability to do so would be dependent upon the terms of the licence agreement entered into with the debtor. Likewise, a debtor possesses no statutory power to terminate IP rights once insolvency proceedings are commenced and its authority to do so would also be governed by the terms of any licence agreement entered into with the licensee.

A liquidator may, with the permission of the court, carry on the business of the debtor for the purposes of the beneficial winding up of the company. The court may also provide by order that property belonging to the debtor is to vest in the liquidator. It would appear that to a limited extent IP rights belonging to a debtor may therefore be used by a liquidator.

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**Personal data in insolvencies**
**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Under the Data Protection (Privacy of Personal Information) Act, (DPA), generally speaking, personal data should only be kept and processed in a manner compatible with the purposes for which it is collected and such purposes should be known to the data subject when the data are supplied. Any use or disclosure of the supplied data must be necessary for the purposes or compatible with the stated purposes. If the data subject is not aware of the purpose at the time the data was collected, then such disclosures are not permitted without further consent. The collection of customer data is not addressed in the DPA.

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**Rejection and disclaimer of contracts in reorganisations**
**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

With the leave of the court, a liquidator now has the ability to disclaim onerous property. Onerous property is defined as an unprofitable contract or assets of the company that are unsaleable or not readily saleable, or that may give rise to a liability to pay money or perform an onerous act. A disclaimer operates so as to determine with effect from the date of the disclaimer, the rights, interests and liabilities of the company in or in respect of the property disclaimed.

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**Arbitration processes in insolvency cases**
**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

The courts of the Bahamas generally seek to encourage use of alternative dispute resolution mechanisms wherever possible. In practice, however, arbitration procedures are seldom invoked to resolve core issues once insolvency proceedings are in progress.

Arbitration proceedings pending at the time a winding-up order is made or a provisional liquidator is appointed would also be subject to an automatic stay. A party desiring to commence or continue such proceedings would require permission from the court. It is nonetheless to

be noted that an arbitration agreement to which the debtor company is a party is not discharged by winding up.

### Successful reorganisations

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

There are no mandatory features that must be included in a plan of arrangement. Reorganisation under both the IBC Act is voluntarily undertaken and is not set up as a general substitute to liquidation. The role of creditors and their classification do not therefore necessarily feature in the process.

The procedures to be followed in carrying out a reorganisation have been addressed in question 11. To this may be added the right of a member of a company to payment of fair value of his or her shares upon dissenting from the plan of arrangement.

### Expedited reorganisations

- 24 Do procedures exist for expedited reorganisations?**

No.

### Unsuccessful reorganisations

- 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

Non-compliance with the statutory preconditions will prevent implementation of a plan of arrangement. These have been discussed in question 11.

The results of failure to perform a plan of arrangement are not expressly addressed in the IBC Act. If the default relates to payment of a debt, unless prohibited under the terms of the plan itself, a creditor would be likely to exercise remedies available to him or her under the general law or pursue winding up.

### Insolvency processes

- 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

The onset of liquidation is brought to the attention of creditors and the wider public through various mandatory advertising requirements. Under the Companies Act, notice of any resolution passed to voluntarily wind up must be published in the gazette (in practice, one of the major daily newspapers). The Winding-up Rules also have strict guidelines governing the advertisement of all petitions and all appointments of liquidators. Additionally, an official liquidator must describe himself as the official liquidator of the debtor company in all correspondence and documents, further bringing notice of liquidation to the attention of creditors and persons dealing with the company.

During either an involuntary or supervised winding up, the court may direct meetings of creditors to be held for the purpose of ascertaining their wishes in relation to the appointment of liquidators and other matters relating to the winding up. Such meetings may be convened and regulated in such manner as the court deems appropriate.

Subject to few exceptions, a liquidator must give creditors a minimum of 28 days' written notice within which to prove their debts or claims. Under the Winding-up Rules, a creditor whose claim or proof has been admitted is also entitled at all reasonable times to inspect the case file and obtain copies of any document. Creditors are likewise generally given seven clear days' written notice of any meeting directed by a judge for the purposes of ascertaining their wishes in respect of matters arising in the winding up, including the appointment of liquidators. The requirements as to written notice of meetings are often fulfilled by advertising notice of any meetings in the local newspapers.

A liquidator in an involuntary winding up is regarded as an officer of the court and is subject to its oversight and control. His or her reporting

obligations will thus frequently depend upon the terms of his or her appointment. Any liquidation scheme addressing payment of any class of creditors, the compromise of claims and other matters affecting the assets of the company is to be submitted to the court for approval. The liquidator must also file in court every six months after winding up has commenced a list of all proofs received by him or her with his or her decisions thereon.

Once liquidation begins, the right to pursue legal redress on behalf of the estate normally vests in the liquidator. This is often expressly addressed in the terms of appointment. Property of a company that comprises a cause of action or other contingent asset which is incapable of being readily realised, may be distributed to creditors or members by means of transferring it to a new company, established for the purpose, and whose shares will be issued to the creditors or members in proportion to their respective rights against the company.

Provided that the plan of arrangement has been approved by the court as required (see answer to question 11) there is nothing that prevents a reorganisation plan from providing for release of liabilities owed by third parties.

### Enforcement of estate's rights

- 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

A creditor may not generally directly pursue remedies belonging to the liquidator. A liquidator may, for instance, sell or dispose of choses in action thereby indirectly allowing a creditor to pursue such remedies. In these circumstances, the fruits of any remedies would belong to the assignee.

### Creditor representation

- 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

In an involuntary or supervised winding up, the court may, if it thinks it expedient, direct meetings of creditors to be held for the purpose of ascertaining their wishes and may appoint a person to act as chairman of such a meeting and require him or her to report on its outcome.

A company about to be wound up voluntarily, or in the course of being wound up voluntarily, may by resolution delegate to its creditors or any committee of creditors the power of appointing liquidators and filling any vacancies in the appointment of liquidators. By similar resolution the power to enter into any arrangement concerning the powers to be exercised by the liquidators and the manner in which they are exercised may also be delegated to a committee of creditors. Any arrangement entered into between a company about to be wound up voluntarily and its creditors is binding on the creditors if accepted to by three-quarters of their number and value.

The new rules also allow for the formation of a liquidation committee which shall comprise not less than three nor more than five creditors. This committee is elected at the first meeting of the creditors. The committee may resolve to appoint a counsel and attorney to give legal advice to the committee. Legal fees and expenses reasonably incurred by the liquidation committee shall be paid out of the assets of the company as an expense of the liquidation.

### Insolvency of corporate groups

- 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

Under the Rules of the Supreme Court actions involving two or more affiliated debtors pending at the same time may be consolidated. This is usually done where some common question of law or fact arises in the actions or where relief claimed arises out of the same transaction or series of transactions. Savings of legal costs and overall administrative convenience are often prominent considerations in the decision whether or not to consolidate.

There are currently no provisions in the Companies Act or IBC Act allowing assets and liabilities of companies within a group to be pooled for distribution purposes. Each member of a group is normally regarded as a separate entity. The situation is different in the case of insurance companies, where a parent and subsidiary may be wound up in conjunction by the same liquidator.

The new rules do allow for greater collaboration with foreign counterparts and contains provisions specifically devoted to international cooperation in insolvencies. These enable various orders to be made in aid of foreign bankruptcy proceedings, including directions for turning over property belonging to a foreign debtor to a foreign administrator. The court is also expressly empowered under the new rules to make a winding-up order in respect of a 'foreign company' that:

- has property located in the Bahamas;
- is carrying on business in the Bahamas; or
- is registered in the Bahamas.

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### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Further to question 2, appeals from final decisions of the Supreme Court lie as of right, provided the appeal is lodged within time. However, if the appeal is out time an extension of time is required. Appeals of interlocutory decisions require leave of the court. There is a requirement to post security for the prosecution of an appeal in the Court of Appeal, and it is typically around \$2,500.

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### Claims

#### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

A liquidator must normally give at least 28 days' notice of any deadline for creditors to prove their debts or claims. The following matters shall be stated in a creditor's proof of debt:

- the creditor's name and address;
- the total amount of his or her claim;
- particulars of how and when the debt was incurred; and
- particulars of the security if any held by the creditor.

The official liquidator may require that a proof of debt be verified by affidavit.

The liquidator must examine every proof of debt lodged and may either admit or reject the claim in whole or in part, or require further evidence in support of it. The liquidator's decision must be given in writing and, if a proof is to be rejected, must provide written reasons for refusal. A creditor that is dissatisfied with the decision of a liquidator in respect of a proof may apply to the Supreme Court to reverse or vary the decision.

There are no provisions preventing the sale or transfer of claims against an insolvent's estate. Creditors are accordingly free to sell or dispose of their claims in a liquidation.

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### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

There are no provisions in either the Companies Act or IBC Act empowering the court to change the rank of a creditor's claim.

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### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Under the Companies Act and the IBC Act the following claims are paid in priority to all other debts, including those which are the subject of security charges:

- costs and expenses of the winding up;
- statutory rates, taxes, assessments or impositions, fees payable under the insolvency acts, duties and penalties under the Stamp Act, licence fees payable under regulatory laws;
- employees' wages, salaries and gratuities; and
- amounts due in respect of personal injuries to workmen accruing before winding up.

After payment of the liquidation costs, the remaining priority debts rank equally among themselves and are to be paid in full. If the assets of the company are insufficient to meet them, they are to be paid *pari passu*.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

All wages of clerks, servants, workmen and labourers for services performed within a specified period prior to the commencement of winding up are regarded as preferred debts under the Companies Act and IBC Act. The period in question is basically four months prior to liquidation for 'clerks' or 'servants' and two months prior to liquidation in the case of 'workmen' and 'labourers'.

Dismissal during a restructuring or insolvency may constitute dismissal for redundancy for the purposes of the Employment Act 1996, giving rise to a claim for statutory redundancy pay. Redundancy pay is recoverable as a debt due by the employee in the Industrial Tribunal or before the courts and is regarded as a preferred debt in a liquidation. The amount recoverable is prescribed by statute and is calculated on the basis of length of years' service and the employee's position at the date of redundancy. Where there are numerous claims for wages owed to employees, it is acceptable for one proof to be made by some person on behalf of all creditors in the class.

The procedure to be followed in terminating an employee for redundancy is addressed in the Code of Industrial Practice made pursuant to the Industrial Relations Act. The code is not legally binding but rather contains a set of best practices to be followed by stakeholders to promote good industrial relations. This recommends consultation between management, the Ministry of Labour and employees or their trade union concerning any impending redundancies. It further suggests that:

- as much advance warning as possible be given to employees of any redundancies;
- consideration be given to introducing schemes for voluntary separation and a phased rundown of employment;
- it be established which employees are to be made redundant and the order of their discharge; and
- assistance be offered in finding alternative employment.

Under the new rules claims for deficiencies in pension schemes are accorded preferred status in liquidations.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Any sum due and payable on behalf of an employee in respect of medical health insurance premiums or pension fund contributions are preferential debts. After payment of the liquidation costs, these debts together with the remaining priority debts rank equally among themselves and are to be paid in full. If the assets of the company are insufficient to meet them, they are to be paid *pari passu*.

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**Environmental problems and liabilities**

- 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

The company through the liquidator remains liable and to the extent that there are damages that are recoverable the Minister of Health may apply as a creditor. If there are assessments that have been levied then they rank in priority as per the answer to question 33.

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**Liabilities that survive insolvency proceedings**

- 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

Upon completion of a compulsory or voluntary winding up, the debtor company is dissolved and removed from the Register of Companies. Dissolution is normally regarded as bringing the legal existence of the company to an end, including for the purposes of liability. Section 272 of the Companies Act nonetheless provides for the liabilities of the company and of its directors, officers and members to survive removal from the register without stating any limitations on scope. While the IBC Act provides for an application to made to restore a company's name to the register, it contains no similar provisions to section 272 of the Companies Act.

Reorganisation at present is not provided as a general substitute for winding up and may be undertaken by solvent companies.

Liabilities may thus survive this process unless creditors concerned have consented to their release. Any plan of arrangement also requires approval from the court.

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**Distributions**

- 38 How and when are distributions made to creditors in liquidations and reorganisations?**

Distributions will be made only where there are sufficient assets to justify this course. A liquidator must give the Registrar of the Supreme Court not more than two months' notice of any intention to declare a dividend. Notice of intention to declare a dividend must also be given by the liquidator to any creditors known to him or her who have not as yet proved their debts. Immediately after expiry of the time fixed for appealing the rejection of any such proofs, the liquidator shall declare a dividend and give notice of the same to each creditor whose proof has been admitted.

The timing of any distributions during a reorganisation will depend upon the terms of the plan of arrangement.

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**Transactions that may be annulled**

- 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Unless approved of by the court, all dispositions of property, effects and choses in action between the commencement of winding up and the order for winding up in a compulsory liquidation or court supervised liquidation are void. Transfers of shares and alterations in the status of members carried out during this period are also void.

Any attachment, distress or execution of a judgment after commencement of an involuntary winding up or supervised winding up is void. Various transactions may also be invalidated on grounds of undue or fraudulent preference, including:

- conveyances, mortgages, deliveries of goods, payments, executions and other acts relating to property belonging to the company; and
- conveyances and assignments of the property or effects of a debtor to trustees for the benefit of creditors.

Apart from the above, under the Fraudulent Dispositions Act every disposition of property made with the intent to defraud and at an undervalue is voidable at the instance of a creditor prejudiced thereby. Any application to set aside the disposition must, however, be brought within two years of the date of the transaction complained of.

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**Proceedings to annul transactions**

- 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

See question 39. Transactions may generally only be attacked by a liquidator, however, if the complaint is based on undue or fraudulent preference it may be impugned by a creditor.

It should also be noted that the new rules expressly creates a number of new fraud-based criminal offences, such as fraud in anticipation of winding up, transactions in fraud of creditors, misconduct in course of winding up and making material omissions in any statement concerning the affairs of the company with intent to defraud creditors or contributories. The 'suspect period' for the offence of committing a transaction in fraud of creditors is the 12 months immediately preceding commencement of winding up.

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**Directors and officers**

- 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

Officers and directors are not generally personally liable for company obligations. However, under both the Companies Act and the IBC Act past or present officers and directors may be compelled to repay monies or contribute to the assets of the company on proof of specified forms of misconduct. Liability arises mainly in relation to the misapplication or wrongful retention of funds and misfeasance or breach of trust. An application for repayment may be initiated by the liquidator, a creditor or a contributory.

Under section 102 of the Companies Act directors may also be liable to repay the company in respect of resolutions passed prior to winding up authorising prohibited share issues, loans, share acquisitions, commissions and dividend payments. Legal proceedings for repayment under the section must be commenced within two years of the resolution complained of.

In addition, past and present directors and officers may be subject to criminal prosecution for prescribed offences in connection with their management of the company's affairs. They likewise owe fiduciary obligations and a duty of care to the company.

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**Groups of companies**

- 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

Generally a parent or affiliated corporation is regarded in law as having a distinct legal personality and therefore it will be uncommon for a parent company or an affiliated corporation to be held responsible for the liabilities of subsidiaries or affiliates. If fraud is proved, however, then the corporate veil may be lifted and liability may attach. If the corporate veil is successfully lifted, the assets of the individual corporate entity become only a part of the pool of assets available from the group to satisfy outstanding liabilities.

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**Insider claims**

- 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

No.

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**Creditors' enforcement**

- 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

Both real property and personal property that is the subject of a security interest may be subject to seizure in the event of a specified default occurring if the document creating the charge provides for this. If seizure is permitted, this will often be done by appointing a receiver after

prior notice of the default has been given to the debtor. If the default is not remedied, the receiver will normally take possession of all assets subject to the security and sell them to satisfy the debt.

There are also rights arising at common law to distrain for rent which is in arrears. This allows a landlord to seize and sell a defaulting tenant's goods to procure rent. The tenant's tools of trade up to a certain value, clothing and other specified goods have traditionally been exempt from seizure.

#### Corporate procedures

##### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Bankruptcies involving individuals are governed by the Bankruptcy Act and the accompanying Bankruptcy Rules. Proceedings are heard by the Supreme Court and may be instituted by one or more creditors in respect of a debt of not less than B\$200 where statutory preconditions are met. Where an individual has been adjudged a bankrupt, the court will summon a general meeting of his or her creditors with a view to securing the appointment of a trustee of the property of the bankrupt and giving directions for the discharge of his or her duties. The Bankruptcy Act enables compositions or arrangements for the settlement of the bankrupt's affairs to be agreed to by the trustee. After the close of the bankruptcy or at any time during its continuance with the assent of the creditors, the court may make an order discharging the bankrupt, upon which he or she shall stand released from most debts provable in the bankruptcy.

The procedures for dissolution of companies are addressed in question 46.

#### Conclusion of case

##### 46 How are liquidation and reorganisation cases formally concluded?

In a compulsory liquidation, after the affairs of the company have been completely wound up, the court may make an order that the company be dissolved. The liquidator then reports the order to the Registrar of Companies, who records the dissolution in the companies register. The case will be treated as being concluded as of the date of the order.

As soon as the affairs of the company are completely wound up in a voluntary winding up the liquidator provides an account of his or her handling of the liquidation, which is laid before a general meeting of the company. He or she then makes a return to the Registrar of Companies confirming that such a meeting was held and, after expiry of three months, the company is deemed to be dissolved. Notification of the dissolution is then given by public advertisement in the gazette and in any local newspaper as determined by the registrar.

Reorganisation is not a general substitute for winding up in the Bahamas and may be undertaken by solvent companies. The process to be followed will ultimately be governed by the terms of the plan of

arrangement approved by the court. As reorganisation is entirely distinct from winding up and may involve no issue of insolvency, the company may continue in existence unless the plan of arrangement calls for otherwise.

#### International cases

##### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

The Bahamas does not currently have legislation in force providing for recognition of foreign insolvency proceedings and office holders. The question of according recognition in such circumstances therefore falls to be determined based on principles of common law.

Courts in the Bahamas normally regard the personal law of a company to be the law of the place of its incorporation. This will therefore be accepted as the law that also governs its dissolution. On this basis, a Bahamian court will accord recognition to a liquidator's appointment under the law of the place of incorporation without the need for formal recognition procedures. Provided it is not prohibited under that law, a Bahamian court will allow the liquidator to bring proceedings on behalf of the company locally to obtain relief ancillary to the foreign winding up. Similarly, assets belonging to the debtor may be vested in the foreign office holder.

The new Rules legislate extensive provisions for international cooperation in insolvency matters in the Bahamas. This enables a foreign office holder to apply for recognition to act in the Bahamas and thereby attain a wide array of 'ancillary orders', including: a stay of proceedings; a stay of enforcement of a judgment; orders requiring the production of information; and orders for the turnover of assets.

Superior court judgments and arbitrators' awards issued in certain jurisdictions may be registered and enforced under the Reciprocal Enforcement of Judgments Act (see question 8). Foreign creditors are not precluded from proving in an insolvency and generally have the same rights as domestic creditors in participating in such proceedings.

#### COMI

##### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

No.



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**Cross-border cooperation****49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

The new Rules empower the court to make wide-ranging ancillary orders in aid of a foreign bankruptcy case. The rules speak to the procedural requirements for invoking the court's assistance. They also specify the considerations that are to influence the exercise of the court's various powers. These include an overriding duty to seek to assure an economic and expeditious administration of the debtor's estate consistent with:

- just treatment of all creditors regardless of place of domicile;
- prevention of preferential or fraudulent dispositions;
- distribution of the estate substantially in accordance with the order of priority that applies locally;
- recognition and enforcement of security interests created by the debtor;
- non-enforcement of foreign taxes, fines or penalties; and
- comity.

Bahamian courts will assist a foreign court in obtaining information or evidence located in the Bahamas that is required for use in pending civil proceedings in another jurisdiction. This is primarily achieved through the Evidence (Proceedings in Other Jurisdictions) Act. The procedure for invoking court assistance involves making an application to a Supreme Court judge.

**Cross-border insolvency protocols and joint court hearings****50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

We are unaware of any arrangements that have been entered into between the Bahamian courts and those of any other jurisdiction to coordinate proceedings. However, the new rules contain provisions addressing international protocols. These make it mandatory for an official liquidator to consider whether it is appropriate to enter into a protocol with a foreign office holder. The stated objective of the provisions is to promote the orderly administration of the estate of a company in liquidation, avoid duplication of work and reduce conflicts between office holders.

# Bahrain

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## Legislation

- 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?**

The Bankruptcy and Composition Law (Law No. 11 of 1987) (the Bankruptcy Law) and Commercial Companies Law (Law No. 21 of 2001) (the Companies Law) comprise the legislation that applies to bankruptcies, reorganisations and insolvency matters in Bahrain. There are separate insolvency rules for financial institutions (commercial banks, investment banks, insurance firms, etc) licensed by the Central Bank of Bahrain (CBB) under the Central Bank of Bahrain and Financial Institutions Law 2006 (the CBB Law). However, the Bankruptcy Law and Companies Law will still apply to such financial institutions to the extent that they do not conflict with provisions of the CBB Law. There are other laws that contain provisions that may indirectly relate to insolvency proceedings including the Civil Code (Law No. 19 of 2001) (the Civil Code) and the Civil and Commercial Proceedings Act (Law No. 12 of 1971).

The principal test determining whether a debtor is insolvent is one that requires the debtor to have experienced financial distress such that the debtor is incapable of paying its debts as they fall due.

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## Courts

- 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?**

The High Civil Court is the court designated to deal with insolvency matters. Appeals can be made to the Court of Appeal. There are no restrictions applicable.

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## Excluded entities and excluded assets

- 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?**

None. Assets owned by the state, however, are excluded from insolvency proceedings and may not be subjected to any interim measures.

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## Public enterprises

- 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?**

See question 26 regarding procedures for insolvent companies. There are no special procedures followed in Bahrain in situations of insolvency of government-owned enterprises. Notwithstanding any insolvent public enterprises that may have governmental ministries, authorities or agencies as its shareholders, public enterprises and any creditors of such public enterprises would be treated like any other company in an insolvency situation.

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## Protection for large financial institutions

- 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?**

No.

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## Secured lending and credit (immoveables)

- 6 What principal types of security are taken on immoveable (real) property?**

The principal types of security for immoveable property are mortgages and pledges. A mortgage is a right acquired by the creditor over the debtor's immoveable asset. The mortgage provides the creditor with priority over any of the debtor's unsecured creditors in relation to the sale proceeds of the immoveable asset. A mortgage over land may be registered with the Survey and Land Registration Bureau and a mortgage over a business may be registered with the Ministry of Industry and Commerce. That said, Bahrain's legal system does not operate in the same way as common law jurisdictions where a security would only be valid and perfected via registration.

A pledge is a right acquired by the creditor to retain or keep possession of an asset of the debtor until such time that the debtor fully repays its debt.

An assignment over a lease or an interest in a parcel of land can also be granted as security.

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## Secured lending and credit (moveables)

- 7 What principal types of security are taken on moveable (personal) property?**

Pledges (as explained above) and rights of retention (or liens) are the principal types of security over moveable property. In addition, a business mortgage can be granted, which will include various moveables belonging to a business including machinery, vehicles, etc. Rights of retention particularly apply where the creditor supplies goods to the debtor. The creditor would have the right to refrain from supplying the goods if the debtor has failed to comply with its contractual obligations.

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## Unsecured credit

- 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

Unsecured creditors may be entitled to interim measures such as obtaining an attachment order from the court over the debtor's assets. The court must be satisfied that there are serious grounds that justify the issuance of the attachment order. Such serious grounds include the risk of the debtor disposing of its assets or acting in a way that would hinder the creditor's right to recourse.

Obtaining an attachment order is not ordinarily a difficult or time-consuming process as such interim measures are filed and heard by the courts on an urgent basis, although each application depends on its facts. There are no special procedures that apply to foreign creditors.

In the context of insolvency, the courts have the authority to preserve the assets of the debtor and a duty to act in the interests of the creditors as a whole. It is therefore possible that an application by an unsecured creditor for an attachment order would be rejected by the courts in the interests of the remainder of the creditors.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

##### Non-financial institutions

The shareholders of a company may, in accordance with the provisions of the company's constitutional documentation, resolve to voluntarily liquidate the company. After completing the necessary filing procedures with the company registrar, the debtor company will be in a state of liquidation, and the powers of the directors will terminate as a result. Upon the conclusion of liquidation proceedings, the debtor company will be removed from the official companies register.

A debtor may also commence its own formal bankruptcy proceedings by submitting a petition to the court, where it has failed to make payment of its debts as a result of a deterioration of its financial affairs. The High Civil Court will issue a bankruptcy order declaring the debtor to be in a state of bankruptcy. A moratorium will thereafter come into effect (see question 15).

##### Financial institutions

An insolvent financial institution that is under administration may, within two years of the date of being placed in administration, submit a petition to the court for its liquidation. A financial institution is deemed to be insolvent if its financial position becomes unstable and it stops paying its due debts other than administrative fines and taxes. The petition must be made available to shareholders and creditors as well as being published in the local newspapers and the official gazette at least 15 days before it is submitted to the court. The court will issue an order declaring the financial institution to be in a state of liquidation, and a liquidator will thereafter be appointed by the CBB.

In addition, a financial institution may resolve to voluntarily liquidate itself without going through the administration procedure by utilising the Bankruptcy Law and complying with the procedure set out above for a non-financial institution, although the CBB would be expected to be involved in the process.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

##### Non-financial institutions

A creditor may file an involuntary application for the bankruptcy of a debtor, where the debtor experiences financial distress such that the debtor is incapable of paying its debts as they fall due. If the court accepts the creditor's application, it will issue an order declaring that the debtor is in a state of bankruptcy. Concerned parties may contest the bankruptcy, by filing a petition within 10 days of the bankruptcy order being published in the local newspaper. Once the bankruptcy order is issued, an automatic moratorium or stay of proceedings will be imposed over the debtor. The court will appoint a bankruptcy trustee, and the powers of the debtor's incumbent board of directors will terminate accordingly.

##### Financial institutions

Creditors of an insolvent financial institution that has been placed under administration may, within two years of the institution being placed in administration, submit a petition to the court for its liquidation. See question 9 for requirements and effects.

Alternatively, creditors of an insolvent financial institution, which is not under administration, may apply to the court by utilising the Bankruptcy Law and complying with the procedure set out above for a non-financial institution, although (as is the case in voluntary liquidations) the CBB would be expected to be involved in the process.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Save for instances of fraud, gross negligence or an act of wrongdoing that would not have otherwise been committed by an ordinary businessperson, a debtor may apply for a scheme of arrangement where his or her business becomes disorganised in such a manner as to lead to a suspension of its payments to creditors. The petition may be filed within 30 days of the date on which the debtor fails to pay its debts. The debtor or the debtor company must prove that it has carried on business continuously during the year prior to the application. In addition, the debtor company must have obtained approval of its shareholders to be able to file the application. Upon filing the application, the debtor must provide the court with its recommendations for reorganisation (and adequate guarantees for its implementation). Following the acceptance of the application, the court will appoint a supervisor and order the commencement of the scheme of arrangement as between the debtor and its creditors. A moratorium will come into effect in relation to any enforcement proceedings against the debtor. The scheme of arrangement is applicable to all creditors whose debts are deemed to be unsecured even if they do not participate in the proceedings or vote for the scheme.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

There is no clear scope under the Bankruptcy Law for creditors to commence reorganisation proceedings against a debtor.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

##### Non-financial institutions

A debtor may be subject to mandatory insolvency proceedings where:

- the predetermined life of the company has expired;
- the company fulfils the purposes and objects for which it was incorporated;
- there has occurred a destruction of the company's assets to such an extent that it would no longer be feasible for the company to carry on;
- the company merges with another company;
- the company fails to carry on any business continuously for a period of one year; and
- the insolvency is in the interests of public policy.

There are no liabilities for failing to commence mandatory insolvency proceedings, as it is normally the court or state regulators that initiate such proceedings where any of the foregoing events take place. If a debtor carries on its business while insolvent, that debtor may face penal sanctions involving either fines or prison sentences if the debtor carried on such business with the intention to defraud creditors as to its solvent state.

##### Financial institutions

The court may order the mandatory liquidation of a financial institution if it is deemed insolvent or if the court finds the liquidation to be just and equitable (eg, the actions undertaken by the institution are harmful to the national economy) or after an administration period has come to an end and the licensee's affairs cannot be restored. Under the CBB Law, the CBB may require a director or employee of an insolvent financial institution to pay compensation if that director or employee permitted the financial institution to carry on business while being aware that it was insolvent.

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**Doing business in reorganisations**


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- 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

A debtor may, in the context of a reorganisation or scheme of arrangement, continue to carry on its business under the supervision of a court-appointed supervisor. The debtor may continue to take such actions it deems necessary, provided that such actions are regarded to be in the ordinary course of business. There are therefore no restrictions on the use of assets in so far as such use is deemed part of the debtor's ordinary course of business. However, the bankruptcy courts will take such necessary measures they deem suitable to preserve the assets of the debtor. The debtor will therefore not be able to sell any assets of its business without the express permission of the relevant bankruptcy court. Moreover, no special treatment is afforded to creditors for the supply of their goods to the debtor after filing. One of the main responsibilities of the court-appointed supervisor is to supervise the manner in which the debtor conducts its business. Any powers held by directors or officers of the insolvent debtor company will be suspended and assumed by the bankruptcy trustee upon an adjudication of the debtor's bankruptcy.

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**Stays of proceedings and moratoria**


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- 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

**Non-financial institutions**

A moratorium or a stay of proceedings would automatically come into force with respect to claims or enforcement actions against the debtor following the commencement of bankruptcy or a scheme of arrangement.

Under bankruptcy proceedings, the issuance of a bankruptcy order has the effect of suspending all payments and imposing a moratorium against the debtor. The moratorium does not extend to secured creditors, who are entitled to pursue their enforcement claims or initiate legal proceedings against the bankruptcy trustee. The bankruptcy trustee may, under the direction of the bankruptcy court, seek to relieve the secured creditors promptly by either immediately repaying the secured debts (in the unlikely event that sufficient funds are available) or procure the secured asset to be sold and repay the secured creditors with the sale proceeds. There are no similar means of relief for unsecured creditors.

**Financial institutions**

As far as financial institutions are concerned a moratorium takes effect on the commencement of administration proceedings. This means that no measures can be taken against the financial institution without the approval of the administrator.

If the financial institution is subject to bankruptcy proceedings without going into administration first, the paragraph relating to non-financial institutions above applies.

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**Post-filing credit**


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- 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

The ability of a debtor to obtain funding or loans in the course of a reorganisation depends on whether such an act is part of the debtor's ordinary course of business. The debtor would otherwise have to obtain the approval of the High Civil Court. Any new loan (whether secured or unsecured) will have no priority and will be excluded from the reorganisation scheme, unless the loans have been obtained within 15 days of the date on which the order for the commencement of reorganisation is published and notice has been provided to the supervisor of the reorganisation proceedings.

**Financial institutions**

In the context of an insolvency of a financial institution, the administrator has powers to obtain unsecured or secured loans.

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**Set-off and netting**


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- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

Set-off rights can be exercised during liquidation or bankruptcy proceedings where the relevant rights and obligations are 'interrelated'. There must be a high level of connection between the rights and obligations that are to be set off.

The extent to which a set-off is exercisable in the course of a scheme of arrangement depends on whether it could be deemed to be in the ordinary course of business. The approval of the bankruptcy judge would be required to the extent that it is not within the scope of the ordinary course of business.

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**Sale of assets**


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- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

**Voluntary liquidation of non-financial institutions**

A company in liquidation may only conduct its business to the extent deemed necessary for the purposes of the liquidation proceedings. A liquidator has the power to sell the company's assets in the manner he or she deems appropriate, unless the liquidator's deed of appointment stipulates otherwise. The liquidator may not proceed with the sale of the debtor's entire assets or entire business without obtaining the approval of the shareholders at a shareholders' meeting. The purchaser will acquire the assets free and clear of claims, unless the assets are encumbered with third-party interests. Unless his or her deed of appointment indicates otherwise, there is nothing that would prohibit the liquidator from employing 'stalking horse' bids in the sale procedure. Moreover, except for instances of fraud or wilful wrongdoing, there is nothing that would limit the liquidator from entering into credit-bidding arrangements with the creditors. If a credit bidder is an assignee of the original secured creditor, there is nothing preventing the liquidator from entering into credit bid arrangements provided any such transaction is not concluded on the basis of 'personal' considerations. Factors that would determine whether any credit bid transaction was tainted with personal considerations include whether or not the transaction was:

- completed at an arm's length;
- a fair market price; and
- in the interest of all creditors.

**Reorganisation of financial and non-financial institutions**

A debtor may not conduct any action that is deemed outside the scope of its ordinary course of business unless it obtains the approval of the bankruptcy judge. As such, a sale of the debtor's entire business may only take place after the approval of the High Civil Court. The purchaser will acquire the assets free and clear of claims, unless the assets are encumbered with third-party interests. There is nothing within the Bankruptcy Law to suggest that 'stalking horse' bids could not be employed. It is more questionable, however, whether the debtor can enter into credit-bidding arrangements, as the debtor is prohibited from entering into transactions that would damage or compromise the position of its creditors.

**Involuntary liquidation of non-financial institutions**

The debtor is restricted from managing or disposing its assets in the course of liquidation proceedings. The court-appointed bankruptcy trustee may, subject to the approval of the bankruptcy judge, proceed with the sale of the debtor's assets where such a sale would be beneficial to the bankruptcy proceedings. For credit bids, no court order will

be required unless the terms of the court-appointed bankruptcy trustee does not include the power to accept credit bids and conclude such transactions. Any such transaction must not be completed on the basis of personal considerations. Factors taken into consideration by a court when assessing any credit bids are similar to those noted above for voluntary liquidation of non-financial institutions.

#### Administration and liquidation of financial institutions

To the extent that the financial institution has been placed under administration, the administrator has broad powers to conclude agreements or take necessary actions that would be in the interests of the financial institution and its creditors. If the financial institution is in liquidation, the liquidator must obtain the consent of the court in respect of the sale of any assets exceeding the value of 100,000 Bahraini dinars. No court order will be required unless the terms of appointment of the administrator requires the administrator to obtain a court order prior to accepting any credit bids. As noted above factors relevant in the context of bankruptcy proceedings equally apply in the context of an administration.

#### Intellectual property assets in insolvencies

- 19** **May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

The IP licence agreement will continue to be enforceable and will be treated like any other legally binding agreement entered into prior to the initiation of the insolvency proceedings. There is nothing in the Bankruptcy Law that limits the ability of the licensor to terminate the agreement. Although the insolvency administrator would be required to safeguard the interests of the debtor, he or she may not continue to use the IP for the benefit of the estate after termination of the licence agreement.

#### Personal data in insolvencies

- 20** **Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

The insolvent company will, even during its reorganisation, remain liable for any transfer of confidential/personal information and/or customer data in its possession, without a valid written consent from the owner of such personal information and/or customer data. Therefore, unless the insolvent company has obtained such written consent from the owner or obtained a court order allowing it to transfer such personal information and/or data, the insolvent company should refrain from doing so.

#### Rejection and disclaimer of contracts in reorganisations

- 21** **Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

A debtor would not be entitled to unilaterally reject or disclaim an unfavourable contract entered into at 'arm's length'. If the unfavourable contract is impossible or excessively onerous for the debtor to perform, then the courts in Bahrain will have the authority, having regard to the interests of both the parties to the agreement, to reduce the obligations of the debtor accordingly. If a contract is breached by the debtor after the adjudication of bankruptcy, the creditor would be unable to raise a claim by virtue of the stay in proceedings imposed by the moratorium (see question 15). The creditor must therefore lodge a claim with the bankruptcy trustee (see question 31).

By contrast, the administrator or liquidator of a financial institution may, subject to the approval of the court, unwind a contract if that is deemed to be in the interests of the financial institution, to protect

the interests of its customers or to avoid the occurrence of irrevocable damages.

#### Arbitration processes in insolvency cases

- 22** **How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

The courts in Bahrain would generally respect the parties' intention to proceed with arbitration in the event of insolvency, where the parties have agreed to this in writing. The approval of the High Civil Court must be obtained if the parties wish to commence arbitration proceedings after the issuance of the bankruptcy order. The Bankruptcy Law does not limit the types of insolvency disputes that may be arbitrated.

#### Successful reorganisations

- 23** **What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

Under a voluntary petition for reorganisation (or scheme of arrangement) a meeting between the debtor and the creditors would have to be convened within 30 days of the date on which the reorganisation was ordered by the court to commence. Participation is limited to ordinary unsecured creditors. Creditors with secured rights over the debtor's assets would be entitled to participate if such creditors are willing to either waive their security or write off a third of the debts owed to them by the debtor. The debtor will present its recommendations on a settlement or reorganisation plan for discussion with participating creditors at the meeting. The reorganisation plan must be approved by the majority of creditors representing one-third of the certified and uncontested debts owed by the debtor. Creditors that did not participate by voting on the reorganisation plan will be excluded for the purposes of calculating the said majority. There are no limitations on the reorganisation plan releasing non-debtor parties. Once approved, the plan will be binding on all creditors.

#### Expedited reorganisations

- 24** **Do procedures exist for expedited reorganisations?**

No.

#### Unsuccessful reorganisations

- 25** **How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

A proposed reorganisation could be defeated where the plan fails to achieve the requisite approval of the creditors present at the meeting (see question 23). More importantly, the High Civil Court must certify any reorganisation plan, and it reserves the authority to reject any plan on the basis of public policy or if the plan is not in the interests of the creditors as a whole. Bankruptcy proceedings may commence in the event that the reorganisation fails to obtain approval.

A failure by the debtor to perform the approved reorganisation plan will result in the termination of the plan, paving the way for bankruptcy.

#### Insolvency processes

- 26** **During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

Notice of the bankruptcy proceedings will be given in the local newspapers. The notice will include an invitation for creditors to submit their claims. Local creditors have a period of 10 days, with foreign creditors

having a period of 30 days, to submit their claims. To the extent that a creditors' union is formed (see question 28), the creditors may hold a meeting to replace the court-appointed bankruptcy trustee. A meeting may also be held for the creditors to discuss the accounts and statements prepared by the bankruptcy trustee in relation to the debtor.

The bankruptcy trustee is required to compile an inventory of the debtor's assets, a copy of which shall be deposited with the High Civil Court and bankruptcy trustee. Such records may be viewed by creditors with the permission of the bankruptcy trustee.

The bankruptcy trustee is required to provide the court with a report of the reasons and circumstances that led to the debtor's insolvency within 30 days of the date of the trustee's appointment. The bankruptcy trustee may be requested by the court to provide reports on the state of bankruptcy on a periodical basis (including monthly reports on any assets that have been collected for the proceedings).

It is the bankruptcy trustee, rather than the creditors, that has the authority to pursue the estate's remedies against third parties. Release of liabilities owed by third parties who are part of the debtor group will only be permitted if the bankruptcy trustee obtains a court order.

#### Enforcement of estate's rights

**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

Only relevant insolvency official is entitled to pursue the estate's remedies or any other rights owed to the debtor. The fruits of any rights or remedies form part of the debtor's pool of assets, and will be distributed as among the creditors.

#### Creditor representation

**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

Under a scheme of arrangement, a creditors' committee can be formed. During bankruptcy, a union of the creditors is formed immediately by law where the debtor has failed to reorganise its debts, the creditors have rejected the debtor's reorganisation plan or the debtor has failed to implement the reorganisation plan. The union includes all creditors (whether secured or unsecured). The union has the power to replace the court-appointed bankruptcy trustee with one that is appointed by a 75 per cent majority. The union has powers to authorise or limit the debtor's ability to carry on new business. It also has the responsibility to supervise the actions of the elected bankruptcy trustee. There are no restrictions on the creditor to retain the services of advisers, but it is unlikely that the expenses can be claimed from the bankruptcy proceeds (unless such advisers were appointed by the High Civil Court).

#### Insolvency of corporate groups

**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

The parent and subsidiary companies are not part of the insolvency proceedings, unless the parent and subsidiary were jointly liable with the debtor in repaying a particular debt, and have become insolvent as a result of their combined failure to repay the same. To the extent that the debtor and its affiliated companies enter insolvency, the bankruptcy trustee may be able to pool the assets of the various entities. Under formal bankruptcy proceedings, the bankruptcy judge would have to approve the wholesale transfer of assets to insolvency proceedings held in another country.

#### Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

A final judgment on a matter in dispute can be appealed to the higher court. The right of appeal is automatic, unless the appeal is filed at the Cassation Court, in which case, a written approval is required to be obtained from the Consulting Chamber of the Cassation Court before the appeal is accepted to be heard.

Yes, there is a requirement to post security to proceed with an appeal but only when the appeal is filed at the Cassation Court. Currently, the fixed amount of security deposit is 50 dinars (approximately US\$135). The deposit is paid along with the court fee of 100 dinars and postal charges of 2 dinars for summoning the parties.

#### Claims

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

##### Non-financial institutions

As indicated above, all creditors are required to submit their claims within 10 days from the date of publication of the bankruptcy order in local newspapers (as opposed to 30 days for foreign creditors (see question 26)). Claims may be contested by the bankruptcy trustee or the creditors, if the claim has not been submitted within the prescribed time frame, or if the claim lacks the necessary documentary evidence. The bankruptcy judge issues a ruling on any creditor claims that have been contested, and the affected parties have the right to appeal.

There are no particular restrictions on a party's right to transfer a claim. A creditor may, in accordance with the provisions of the Civil Code, assign its right to a claim to a third party. The Civil Code permits a creditor to claim for contingent liabilities where the claim is reliant on a future event that is deemed to be certain.

Once creditors submit their claims, the bankruptcy trustee will be involved in verifying the amounts using the documentary evidence provided (loan documents, agreements, certificates, etc).

There is nothing in the Bankruptcy Law that would prohibit a claim acquired by another at a discount to be enforced for its full face value provided a creditor can verify that the insolvent debtor owes such a debt at full face value.

The Bankruptcy Law suspends the accrual of interest over a creditor's claims upon the court's adjudication of bankruptcy.

##### Financial institutions

Creditors of an insolvent financial institution will be invited by the liquidator to submit their claims within 60 days from the date of receiving notification thereof (see question 26). Creditors will have a right to appeal a decision by the liquidator to reject their claims.

#### Modifying creditors' rights

**32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

Yes, if the court considers that security is defective or if security is granted during the 'suspect period' (see question 40).

#### Priority claims

**33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

##### Non-financial institutions

Apart from employee-related claims (see questions 34 and 35), sums due to the state (whether taxes, duties or otherwise) and the costs associated with the sale of the debtor's assets have a privileged

status and therefore retain priority over the debtor's secured and unsecured creditors.

#### Financial institutions

The CBB Law provides priority to the fees and expenses of the administrator and liquidator, followed by taxes due to the government, deposits and loans taken with the approval of the CBB to keep the financial institution from insolvency, deposits not exceeding 20,000 Bahraini dinars and deposits exceeding the foregoing amount.

#### Employment-related liabilities in restructurings

##### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

An employer is entitled to dismiss its employees in the event of a restructuring or as a result of severe financial difficulties. The employer would nevertheless be liable to pay the employee his or her wages up to the date of dismissal, any accrued annual leave, any benefits promised under the employment contract and, in some particular cases, a compensation sum for the employee's time in service (known as a leaving indemnity). The employer must abide by its obligation of serving the employee a minimum of one month's notice (or such other period of notice stipulated in the employment contract).

The employer does not incur additional liabilities on account of dismissing a large number of employees.

#### Pension claims

##### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

In Bahrain, employee pensions tend to be administered by the state under the auspices of the Social Insurance Organisation. It is possible for employers to operate private pension schemes for their employees in Bahrain, although this remains a rarity. That said, an employee's entitlement under a private pension scheme will enjoy a privileged status over the claim of any creditors.

#### Environmental problems and liabilities

##### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Legislative Decree No. 21 of 1996 in respect of the Environmental Law requires a person to repair, rectify or reinstate any damages or losses caused by that person to the environment in Bahrain. The law does not take into account any insolvency scenarios and does not expressly state that such environmental liability may be shared with other non-offending parties. More importantly, the environmental liability is owed to the government (and in particular, to the Supreme Council for the Environment). Accordingly, the courts in Bahrain may treat this government-owed environmental liability as a priority claim over all other secured and unsecured claims (see question 33).

#### Liabilities that survive insolvency proceedings

##### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Criminal liability, claims against directors under the Companies Law, claims relevant to the assets and disposals not covered by the prohibition imposed upon the bankrupt, and claims relating to the business of the bankrupt that the debtor is permitted to perform under law would survive insolvency or reorganisation.

#### Distributions

##### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Distributions are made by permission of the High Civil Court once the list of creditors (and their respective claims) has been finalised, and the

pool of the debtor's assets has been ascertained (whether through sale or otherwise). Privileged creditors are the first to be paid as a matter of priority. Secured creditors will have their debts repaid from the sale proceeds of the secured asset, and any profits obtained from the sale shall be distributed among the unsecured ordinary creditors. The unsecured creditors will rank equally in claiming any of the debtor's remaining assets.

#### Transactions that may be annulled

##### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

#### Non-financial institutions

Under the Civil Code, a creditor may claim to have a transaction entered into by the debtor set aside where the transaction has the effect of increasing the debtor's financial obligations and the parties to the transaction were aware of the debtor's state of insolvency. Moreover, a transaction entered into by the debtor may be declared void if it provides an 'unjustifiable preference' to a third party or if it was entered into under fraudulent circumstances.

A bankruptcy trustee may also seek the avoidance of a transaction entered into by the debtor during the course of bankruptcy if the effect of the transaction is based on personal consideration.

Any benefits transferred under a void transaction will be redeemed and will be shared by the creditors.

The following disposals may be annulled or set aside if effected by the debtor after the date of suspension of payment (see question 40) and before the adjudication of bankruptcy:

- all donations other than small presents that are customary;
- any kind of premature discharge of debts, the creation of a consideration for the discharge of an unmatured negotiable instrument will be deemed as a discharge;
- payment of maturing debts other than by the manner agreed; and
- any mortgage or other agreed security imposed upon the debtor's assets to secure a previous debt.

Further, disposals other than those mentioned above performed within the time limit stated therein may be adjudged as invalid against the body of creditors where the disposal is detrimental to them and the disposing party was aware at the time of the disposal of the bankrupt's suspension of payment.

#### Financial institutions

An insolvent financial institution is deemed to have entered into a void transaction within the suspect period (see question 40) if:

- the transaction was at an undervalue;
- the transaction was entered into with the purpose of defrauding any of the financial institution's creditors; or
- the transaction gave a preference to any person.

#### Proceedings to annul transactions

##### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

#### Non-financial institutions

Under the Bankruptcy Law, the court can set a date that will be considered as the date of suspension of payment, but this date cannot be backdated to more than two years from the date the debtor is adjudged bankrupt. The period from the suspension of payment until the adjudication of bankruptcy is referred to as the 'suspect period' and the court may consider disposals or transfers within the suspect period to be void if they are detrimental to creditors.

#### Financial institutions

A suspect period is applicable in the context of an insolvent financial institution that has entered into a void transaction (see above). More particularly, the suspect period is two years from the date of the financial institution being placed under administration or from the date

on which the liquidation order was issued where the void transaction is with a related party (directors, officers, etc). A suspect period of six months applies from the date of the financial institution being placed under administration or from the date the liquidation order was issued where the void transaction is entered into with anyone other than a related party.

#### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

##### Non-financial institutions

If the company's assets or remedies are insufficient to repay 20 per cent of its outstanding debts, the High Civil Court may order the shareholders and directors, either jointly or severally, to pay all or part of the company's debts, unless the shareholders and directors can prove that they have acted in accordance with the standards of a 'reasonable man'. Moreover, the Companies Law states that the board will be jointly liable before the company, the shareholders, and any third parties for all acts of fraud, misuse of power, mismanagement or violation of the law and the company's articles. In this respect, directors may be liable for approving a voidable transaction (see question 39) that has caused losses to the company's creditors.

##### Financial institutions

In addition to the above, a director of an insolvent financial institution that carries on its licensed activities knowing (or where he or she should have known) that the institution is insolvent will be liable to a term of imprisonment and a fine not exceeding 20,000 Bahraini dinars.

#### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

See question 41 for instances where shareholders (parent companies) may be held liable for the obligations of the insolvent company. Parent or affiliated corporations may also be held liable where they have provided guarantees or have acted in the capacity of sureties with regard to the insolvent company (see also question 26). Unless shareholders (or parent companies) have provided guarantees to support its subsidiaries, a court would not order a distribution of group company assets pro rata without regard for the assets of individual corporate entities involved.

#### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

No. All creditors are allowed to submit their claims against an insolvent debtor under Bahrain's insolvency laws, even when there is some degree of proximity between the creditor and insolvent debtor (ie, in the case of insiders). Nevertheless, creditors that have entered into non-arm's-length transactions with the insolvent debtor are susceptible to being challenged by the bankruptcy trustee or administrator on grounds of preferential treatment (see question 39).

#### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

It is unlikely that there will be concurrent processes in which the debtor's assets would be seized outside of court proceedings, as the High Civil Court retains ultimate authority in preserving the assets of the debtor and acting in the interests of the creditors as a whole. The bankruptcy trustee would have the authority to claw back seized assets where there is sufficient proof to suggest that the debtor has a legal right to the assets.

#### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

The Bankruptcy Law includes discrete provisions that apply to corporations but the entire Bankruptcy Law will apply to corporations as long as they do not conflict with the relevant provisions relating to corporations.

#### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Liquidations and bankruptcy proceedings are formally concluded with the liquidator or bankruptcy trustee presenting his final report on the debtor to the court. The court would certify the report and order for distributions to be made among the creditors. Similarly, a scheme of arrangement would be formally concluded once the reorganisation plan, backed by the majority of the creditors, is sanctioned by the High Civil Court.

#### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

A judgment or award issued by a foreign court will be recognised in Bahrain if the foreign court shares a reciprocity arrangement with Bahrain. In addition, the judgment must comply with the conditions of the Civil and Commercial Procedures Act, which provide that:

- the Bahrain court did not have jurisdiction in the matter in respect of which the order or judgment was made and it was made by a foreign court of competent jurisdiction under the jurisdictional rules or laws applied by such courts;
- all parties were served due notice to attend and had been properly represented;
- the order or judgment was final in accordance with the laws of the court making it (regardless of whether such order or judgment is subject to appeal to a higher court); and
- the order or judgment of the foreign court does not conflict with any previous decision of the Bahrain courts and does not conflict with public policy or morality in Bahrain.

Bahrain has not adopted the UNCITRAL Model Law on Cross-Border Insolvency.

#### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

As far as we are aware, the courts in Bahrain have not adopted nor applied any COMI tests for debtor companies. Accordingly, COMI has no practical application in Bahrain (see also question 47 concerning the UNCITRAL Model Law on Cross-Border Insolvency).

**Cross-border cooperation**

- 49** Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

There are rules in place for cooperation with the courts of the Gulf Cooperation Council (GCC). However, with respect to non-GCC countries, we are not aware of systems that would allow cooperation between domestic and foreign courts. Generally, the courts will refuse to cooperate with foreign proceedings or foreign courts particularly when such proceedings do not comply with the conditions described in the response to question 47.

**Cross-border insolvency protocols and joint court hearings**

- 50** In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

None that we are aware of.



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# Belgium

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Act of 8 August 1997 on Bankruptcies (the Bankruptcy Act) governs bankruptcies of commercial entities or individuals carrying on commercial activities. Judicial reorganisations and amicable settlements of commercial entities or individuals carrying on commercial activities are governed by the Act of 31 January 2009 on the Continuity of Undertakings (the Continuity Act).

The Act of 25 April 2014 on the status and supervision of credit institutions and the Act of 13 March 2016 on the supervision of insurance undertakings contain specific provisions relating to the reorganisation and winding up of credit institutions and of insurance undertakings respectively.

The Belgian Companies Code contains provisions applicable to the voluntary winding up of companies.

Belgian law has no general criteria to determine whether a debtor is insolvent. Each regime (bankruptcy and judicial reorganisation) has different criteria to make this assessment. The Bankruptcy Act applies from the moment a debtor has consistently ceased to pay its debts when they fall due and no longer has the trust of its creditors. A debtor can apply for a judicial reorganisation when the continuity of that debtor's business seems to be threatened in the long or short term.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The relevant court in bankruptcy and judicial reorganisation proceedings is the commercial court of the place where the debtor:

- if it is a company, has its registered office; or
- if it is an individual, has his or her main place of business at the time the proceedings are commenced.

The commercial court has jurisdiction over the opening of insolvency proceedings and over any disputes arising from the insolvency.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The Bankruptcy and Continuity Acts do not apply to entities or individuals whose trade or profession does not involve them in commercial activities. Private individuals not involved in commercial activities may, under certain conditions, apply for a collective debt rescheduling under the Act of 5 July 1998 on Collective Debt Rescheduling. Insolvency situations affecting other non-commercial entities are not specifically regulated. Belgian law nevertheless contains a general principle of equal treatment of creditors. This principle mandatorily applies to all situations where two or more creditors concurrently seek recourse to their debtor's assets. The principle of equal treatment will thus apply both in the event of an attachment of assets by several creditors and in the event of a voluntary winding up or liquidation of a corporate entity.

The Belgian Judicial Code enumerates a certain number of assets that are excluded from insolvency proceedings involving an individual. Legal entities do not benefit, in principle, from such protection and none of their assets are thus exempt from claims of creditors.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The fact that an enterprise is government-owned does not in itself mean that such enterprise would not be subject to the Bankruptcy Act or the Continuity Act. The latter will depend on whether or not the enterprise primarily engages in commercial activities.

There are a number of caveats here. Certain public entities that clearly perform commercial activities (eg, Belgacom, SNCB, Bpost) are not subject to the Bankruptcy Act (but can become subject to the Continuity Act). Other exemptions may also exist in specific legislation governing certain government-owned enterprises.

In general, creditors of insolvent government-owned enterprises may attach (which can lead to a forced sale of) the assets of a government-owned enterprise to obtain payment of their claims. However, such attachment is limited (ie, assets that such entities use entirely or partially within the framework of their public services are excluded from attachment procedures or other insolvency proceedings (sovereign immunity from enforcement)).

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Belgium has introduced new banking legislation in line with the European regulatory framework (Capital Requirements Directive IV 2013/36/EU CRD IV, single supervisory mechanism, Bank Recovery and Resolution Directive (2014/59/EU) (BRRD) and prohibition (subject to exceptions) of proprietary trading).

The new banking legislation consists of four new laws: the Law of 25 April 2014 on the status and supervision of credit institutions, the Law of 25 April 2014 containing various provisions, the Law of 25 April 2014 establishing mechanisms for a macro-prudential policy and outlining the specific tasks assigned to the National Bank of Belgium (NBB) as part of its mission to contribute to the stability of the financial system and the Act of 8 May 2014 on appeals against macro-prudential recommendations of the NBB.

Key elements of the reforms, taken together, are the following:

- Effective since 4 November 2014, significant credit institutions (see article 6 of Regulation EC 1024/2013 conferring specific tasks on the European Central Bank concerning policies relating to the prudential supervision of credit institutions) will become subject to the direct supervision of the European Central Bank, which will apply both the European and Belgian rules. New credit institutions will require the approval of the European Central Bank, irrespective of their size.
- Effective since 1 January 2015, credit institutions (that can make an appeal on the Belgian deposit guarantee scheme) will be prohibited from proprietary trading under their trading book. There are a

number of exceptions, such as market making or hedging activities as further determined by the regulator (NBB).

- Additional requirements are imposed on managers and board members. In particular the role of the board as key player in the control, orientation, risk management and compliance of the credit institutions has been enhanced.
- The equity structure of a credit institution consists of 'core equity tier 1', 'tier 1' and 'tier 2'. By 2019, a 'capital conservation buffer', a 'countercyclical capital buffer' and an equity buffer for credit institutions of worldwide or domestic systemic importance is contemplated.
- Credit institutions are required to put in place recovery plans covering different hypotheses and allowing credit institutions to recover, without impact on the financial system, their viability or financial positions.
- Effective since 3 March 2015, resolution mechanism in case of risk of default of credit institutions in order to ensure continuity of the critical functions of credit institutions, avoid systemic risk, protect state resources and protect deposits.

### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

The most important form of security over immoveable property is the mortgage, which provides the mortgagee with the right to have the property sold if the debtor defaults and to use the proceeds of sale to repay the outstanding secured debt.

The creation and perfection of a mortgage requires notarised documents to be filed with the land registry and attracts stamp duty of 1 per cent of the secured amount in addition to various fees. More sophisticated creditors accept an irrevocable mortgage proxy to secure part of the amount as opposed to an effective mortgage, in particular where the secured amounts are substantial. Under such proxy, the owner of the property appoints a third party related to the creditor as its attorney with the power to create an effective mortgage upon the creditor's first demand. The advantage of an irrevocable mortgage proxy is that it does not attract stamp duties other than nominal fees. The disadvantage, however, is that the irrevocable mortgage proxy does not create effective security.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The principal and most traditional type of security over moveable assets is the pledge, which provides the pledgee with the right to have the assets sold if the debtor defaults (subject to the authorisation of the courts) and to use the proceeds of the sale to repay the outstanding secured debt. For a pledge to secure commercial debts, it is necessary to have a pledge agreement as well as the physical transfer of possession of the pledged asset to the secured creditor or to a third party acceptable to both pledgor and pledgee.

The Financial Collateral Act of 15 December 2004 (the Financial Collateral Act) contains simplified rules for the creation, perfection and enforcement of a pledge over financial collateral. These rules apply to cash on account (ie, not physical cash) as well as to financial instruments. The definition of financial instruments covers shares and bonds, but also derivative contracts, dematerialised and book entry securities as well as any right to financial instruments.

The pledge must be agreed in writing and the financial collateral, over which a pledge is created, must be delivered to the beneficiary of the pledge or to the person acting on its behalf. This requirement is met when the financial collateral has effectively been transferred, held, registered in a register or otherwise designated as such, so that the beneficiary of the security acquires possession or control of these assets.

There is no notification requirement or court authorisation procedure for the enforcement of a pledge over financial collateral. If the pledgor defaults, the pledgee has the right to sell the financial instruments or to apply the cash to satisfy the claims it has against the pledgor. The pledgee also has the right to appropriate the financial collateral but only if the parties have expressly agreed thereto and have provided a contractual mechanism for the valuation of the financial instruments. The occurrence of a bankruptcy does not affect the enforceability of a

pledge on financial collateral. However, following a recent amendment to the Financial Collateral Act, certain pledges on financial collateral cannot be enforced anymore during a judicial reorganisation procedure. This is the case for pledges on bank account and credit claims and netting arrangements involving a debtor that is not a public or financial entity, or if the debtor is a public or financial entity, the enforcement can only be requested by creditors that are public or financial entities, except in both cases in the event of default of the debtor. In practice, this means that if the judicial reorganisation proceedings are commenced by a debtor other than a public or financial entity, creditors are not entitled to enforce their security interests or carry out netting arrangements on the sole ground that such proceedings have been opened.

Given the obvious inconvenience caused by the necessity to transfer possession as required for a pledge, Belgian law has introduced the *pand handelszaak* or *gage sur fonds de commerce*, a form of security interest similar to the floating charge under English law. This floating charge covers all business assets of the chargor with the exception of immoveable property and 50 per cent of the value of the stock. The creation of a floating charge requires a written agreement that must be filed with the land registry and that attracts a stamp duty of 0.5 per cent of the value of the assets covered by the floating charge. A floating charge may only be created to secure borrowings from an EC credit institution, or by certain other types of financial institution.

In the event of insolvency, an unpaid seller has a statutory lien on the asset sold to the insolvent buyer, provided, however, that the buyer is the owner of the asset at the time of occurrence of the insolvency event and that the asset is clearly identifiable at that time.

For many years it was unclear whether Belgian law accepted the fiduciary transfer of title. In the *Sart-Tilman* case, the Belgian Supreme Court upheld the decision of the Court of Appeal of Liège, ruling that the security assignment of a claim was ineffective in the event of the insolvency of the assignor. It appears to be widely accepted among scholars that this decision only affects arrangements where the transfer was solely effected for the purpose of creating security and does not affect more complex and well-established arrangements where the use of title as security is only one of the aspects, or one of the consequences (eg, leasing or factoring) of the transaction. The exact scope and effects of the *Sart-Tilman* case are still a source of dissension and legal uncertainty under Belgian law. In 2010, the Belgian Supreme Court held that an ineffective security assignment should be reclassified as a pledge. Special 'protective' legislation exists in respect of 'repo' transactions and transfers of book entry securities and cash. This protective legislation has now been updated and amended in the Financial Collateral Act. The law recognises the validity and the enforceability of a transfer of title to financial collateral by way of security. The fiduciary transfer of title is thus valid under Belgian law and is enforceable, including in the context of insolvency proceedings affecting the debtor that has transferred financial collateral to its creditor by way of security in accordance with the Financial Collateral Act. Recent case law has clarified that the beneficiary of security by way of transfer of title will be in the same legal position as a pledgee in a situation of *concursum creditorum*.

Retention of title arrangements covering moveable property are effective in the event of insolvency affecting the buyer, provided that they meet certain requirements, such as a written agreement executed prior to the delivery of the goods and the availability of the asset in the buyer's estate at the time of executing the retention right, and provided that any maintenance costs have been settled with the bankruptcy trustee.

In 2013, the Belgian Civil Code with respect to security interests over moveable assets was amended. Following the reform, there is one uniform legal framework for pledges a pledge over a company's entire business (*pand handelszaak* or *gage sur fonds de commerce*) is no longer subject to a separate legal framework. The reform will enter into force on a date to be specified by way of a royal decree and at the latest, on 1 January 2018.

One of the main changes introduced by the new legal framework is that dispossession of the pledged assets will no longer be a perfection requirement for a pledge (although the option of dispossession will still remain available). The pledgor may thus remain in control of the assets and continue to use or operate them. The pledgor has to take care of the assets as a 'good pledgor' and is entitled to a reasonable use of the pledged assets in line with their purpose. The parties can agree to limit the pledgor's rights in this respect. The pledgee has the right to inspect

the pledged assets at any time. If the pledgor fails to comply with its obligations in a serious manner, the pledgee may apply to the court to have the pledged assets transferred to it or to a judicial custodian.

Registration of the pledge arrangement in a centralised pledge register will be required to make the pledge enforceable with regard to third parties. The moment of registration will determine the ranking of the pledge arrangement. Each registration will be valid for a renewable period of 10 years and may have to be updated, for example, if the pledge is transferred to a different pledgee pursuant to a transfer of the secured obligations. The specifics of the registration procedure will be set out by separate Royal Decree.

Another noteworthy change is the introduction of a 'security agent' concept similar to the concept already included in the Financial Collateral Law (which is not affected by the new law). In the new legal framework, a representative will be able to enter into a pledge agreement in his or her own name but for the account of one or more beneficiaries. The latter have to be identified or identifiable.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Prior to the commencement of insolvency proceedings, unsecured creditors can enforce their rights against a defaulting debtor by obtaining a court order attaching a schedule of the debtor's assets and requiring them to be sold. A distinction should be made between a pre-judgment conservatory attachment (which, for moveable properties, can be obtained within days in cases of real urgency; for immovable properties, it can take up to approximately one month) and a post-judgment enforcement attachment (which requires either an enforceable judgment to have been made or a notarised deed that details the exact amount due to the creditor). At the time of the commencement of a judicial reorganisation or bankruptcy, attachment and other enforcement measures against the defaulting debtor will be suspended (see questions 11 and 15).

Foreign creditors are treated in the same way as Belgian creditors in a Belgian insolvency, although note that:

- when taking legal proceedings in Belgium foreign creditors can be required, to the extent no particular treaty exemption applies, to put up a bond or collateral to cover the amounts that could become due as a consequence of the proceedings (*cautio iudicatum solvi*); and
- other than to the extent enforcement is recognised under EC Council Regulation No. 1215/2012, a creditor can only proceed to enforcement of a foreign judgment (including attachments) if a Belgian court has made an *exequatur* order (ie, a formal recognition of the judgment and confirmation that it is enforceable in Belgium).

Exceptionally, a foreign creditor's claims may be barred or reduced in insolvency proceedings if the court finds that it has recovered assets abroad in breach of the equal treatment of creditors' provisions.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A voluntary winding up takes place when the general assembly of a company's shareholders decides to dissolve the company in accordance with its corporate charter. Generally, such a decision requires the same quorum and majority as is required for any change to the by-laws of the company. The only exception to this rule applies when the company has lost more than three-quarters of its share capital, in which case the decision to dissolve the company can be taken by one-quarter of the members present or represented at the general assembly.

Following the decision to dissolve the company, one or more liquidators must be appointed to manage the liquidation of the company. The appointment of the liquidators must be confirmed by the court and from that moment the company will be deemed to continue to exist for liquidation purposes only.

As from the date of the decision to dissolve the company, all unsecured creditors are entitled to equal treatment, meaning that they will receive payment of their debts on a pro rata basis.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Under the Continuity Act, creditors can request the court to terminate any ongoing judicial reorganisation proceedings when it is manifest that the debtor can no longer preserve the continuity of its business. In that case, the court may decide to declare the debtor bankrupt or to force the debtor into judicial liquidation proceedings.

Under the Bankruptcy Act, creditors are entitled to place a debtor in bankruptcy by serving a writ of summons before the commercial court. Petitioners are required to demonstrate that the conditions for bankruptcy are met, that is, that the debtor has ceased in a persistent manner to pay its debts, and is no longer able to obtain credit.

In situations of extreme urgency, a creditor may also make an *ex parte* application for an order that the debtor is no longer entitled to manage its assets for a period of 15 days, after which a formal request for bankruptcy must be submitted to the court.

In the case of bankruptcy, the entire estate of the company or the individual will be liquidated. Once the available assets of the company have been fully realised (whether or not they are sufficient to meet its outstanding debts), it will cease to exist by operation of law. If the debtor is a physical person, he or she may be discharged by the court for the unpaid debts remaining after the liquidation.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The Continuity Act provides for two types of financial reorganisations: an amicable settlement without any court involvement and judicial reorganisation proceedings under the supervision of the courts.

#### Amicable settlement

Any debtor can enter into an amicable settlement with some or all of its creditors to address a difficult financial situation or to reorganise its business. The parties to this amicable settlement are free to determine its content but the amicable settlement does not affect the rights of third parties. Under the Continuity Act, the debtor can file a copy of the amicable settlement with the court registry. The purpose of such filing is to protect the terms of the settlement and the transactions concluded under it against certain effects of the 'suspect period' (see question 38). In other words, the Continuity Act provides a safe haven against the risk of the amicable settlement and the related transactions being set aside in a subsequent bankruptcy proceeding.

#### Judicial reorganisation

The aim of a judicial reorganisation is to maintain, under the court's supervision, the continuity of all or part of the debtor's business or of its activities. Judicial reorganisation proceedings can only be started if the continuity of the debtor's business is threatened in the short or long term. A company meeting the conditions for bankruptcy can also be the subject of a judicial reorganisation procedure (see question 1). The judicial reorganisation involves a moratorium granted in favour of the debtor for a period of up to six months. During this moratorium period, no enforcement can take place in principle against the debtor's assets and no bankruptcy proceedings can be opened in respect of the debtor. The three new court-supervised reorganisation processes are as follows.

#### Judicial reorganisation by way of amicable settlement

The negotiations of this settlement take place under the court's supervision. In line with the principles of the Civil Code, the court can sanction a payment deferral. Once agreed, the amicable settlement will be presented to the court and the moratorium will end. Once sanctioned by the court, the amicable settlement is protected against certain effects of the suspect period in the same way as the ordinary amicable settlement.

#### Judicial reorganisation by way of collective agreement

A judicial reorganisation by way of a collective agreement starts with a verification of all claims to be included in the reorganisation plan. As such, the debtor will prepare a reorganisation plan involving a

description of the restructuring and a description of the creditors' rights following the implementation of that restructuring. Certain secured creditors may see their payments deferred and enforcement rights suspended as a consequence of the reorganisation plan for a period of up to 24 months on the condition that they continue to be paid their interest during this period. The reorganisation plan is then submitted to a vote and must be approved by more than half of the creditors representing more than half of the principal amount of the claims involved. If the plan is approved and is deemed to be in agreement with public policy, the court will sanction the reorganisation plan and the moratorium will end. The debtor will then be required to implement and comply with the reorganisation plan and if he or she fails to do so, the creditors may require the court to revoke its approval of the reorganisation plan.

#### ***Judicial reorganisation by way of a transfer of business under court supervision***

The court can order the transfer of all or part of the business of the debtor either with or without the debtor's consent at the request of any interested party if the debtor is bankrupt or if an attempted reorganisation of the debtor has failed.

#### **Involuntary reorganisations**

##### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

A request for a judicial reorganisation procedure can, in principle, only be filed by the debtor. There are, however, two important exceptions to this principle.

- The public prosecutor, a creditor or any interested buyer can ask the court to transfer all or part of the debtor's business, if:
  - the debtor is bankrupt and has failed to file a request for a judicial reorganisation;
  - the court refuses to grant a judicial reorganisation procedure or decides to close it before it is completed;
  - its creditors do not approve the reorganisation plan; or
  - the court refuses to ratify such reorganisation plan.
- If the debtor's obvious and serious defaults are threatening the continuity of its business, every interested party can ask for the appointment of a court representative, who will be required to file, on behalf of the debtor, a request for a judicial reorganisation procedure.

Further, the auditor of a company will be required to inform the board or management body of that company of any material circumstances that might jeopardise the company's continuity. If the company does not take any measures to remedy the situation, the auditor may inform the court thereof.

#### **Mandatory commencement of insolvency proceedings**

##### **13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

The debtor is under a legal obligation to file for bankruptcy within one month of such time as it has consistently ceased to pay its debts and no longer has the trust of its creditors. If the debtor is a company, the decision must be taken by the board of directors unless stipulated otherwise in its articles of association.

If proceedings are not commenced within such time limit, the debtor may be subject to both criminal and civil liabilities. In practice, criminal sanctions will not be ordered for the sole fact of not having filed for bankruptcy in due time. Civil sanctions are, however, significant, since directors may be held personally liable for the increase of the liabilities resulting from the delay in filing for bankruptcy.

#### **Doing business in reorganisations**

##### **14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

The court will in principle allow the debtor to continue operating its business during the moratorium period. The debtor (or its managing bodies) may nevertheless be precluded by the court from performing any act of management if its obvious and serious mismanagement is threatening the continuity of its business. In that case, an administrator will be appointed to continue the judicial reorganisation procedure and the debtor (or its managing bodies) will cease to be involved during the reorganisation.

In principle, all ongoing contracts (ie, contracts existing before the commencement of the proceedings but that provide for further performance by the parties) will continue in effect notwithstanding the judicial reorganisation, but may be terminated during the judicial reorganisation by the counterparty to the extent that the debtor defaults. Note that a contractual default by the debtor occurring before the opening of the reorganisation procedure cannot be considered a valid reason for the counterparty to terminate the contract to the extent that the default is remedied within 15 days of the default being notified to the creditor. The debtor may, within 14 days of the opening of the judicial reorganisation proceedings, decide to cease to perform its obligations under the relevant contract (other than employment contracts) during the moratorium if necessary for the purposes of the reorganisation plan or for transfer of the business.

In order to support the debtor in securing further business and credit, the judicial reorganisation legislation provides that debts arising during the judicial reorganisation period (including claims arising from new agreements as well as claims in relation to agreements for periodically renewable performance or services) will be treated preferentially over all other creditors in the event of a subsequent bankruptcy or liquidation. In addition, new claims arising out of performance after the opening of judicial reorganisation proceedings are not subject to the moratorium. If the debtor fails to pay amounts due in respect of such performance after the opening of judicial reorganisation proceedings, the relevant creditor will have the ability to enforce.

#### **Stays of proceedings and moratoria**

##### **15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

###### **Liquidation**

The immediate effect of the declaration of insolvency is that any legal or enforcement proceedings are suspended. Secured creditors can only commence or continue enforcement proceedings subject to limits set by the bankruptcy legislation.

###### **Reorganisation**

In the case of a request for a judicial reorganisation, no enforcement of any security can be effected nor can the debtor be declared bankrupt or liquidated prior to the court's ruling on such request. The judicial reorganisation involves a moratorium granted to the debtor for up to six months (see question 11).

During this moratorium period, no enforcement can take place in principle against the debtor's assets and no bankruptcy proceedings can be opened in respect of the debtor. Creditors will, however, be able to effect set-off, enforce security over financial collateral and enforce receivables pledges. This moratorium does not affect the ongoing contracts but the debtor can decide, even if not allowed contractually, not to perform the obligations under the relevant contract (other than employment contracts) during the moratorium if it is necessary for the purposes of the reorganisation plan or for the transfer of the business (see questions 37 and 38).

The moratorium period will end and the creditors will, in principle, regain their full rights and may proceed to the enforcement of their rights (including the security) against the debtor, if:

- the reorganisation is unsuccessful (see question 24);
- an agreed amicable settlement is presented to the court (see question 11);
- a reorganisation plan approved by more than half of the creditors (representing more than half of the principal amount of the claims involved) is ratified by the court; however, depending on the content of the reorganisation plan, certain secured creditors can see their payments deferred and enforcement rights suspended for up to 24 months (see question 11); and
- the reorganisation procedure is terminated following the completion of the sale of the business.

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#### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

##### Liquidation

Secured or unsecured loans or credit granted after the commencement of bankruptcy or liquidation proceedings will receive preferential treatment over other claims to the extent that they can be considered as administrative expenses. The Belgian Supreme Court has defined administrative expenses as debts contracted by the bankruptcy trustee for the purposes of the administration of the bankrupt estate.

##### Reorganisation

Claims arising from transactions entered into after the commencement of judicial reorganisation proceedings will be considered as administrative expenses in a subsequent bankruptcy or liquidation and will be treated as a preferential claim.

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#### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Pursuant to the Financial Collateral Act, creditors can exercise the right of set-off following the opening of bankruptcy or judicial reorganisation proceedings unless to the extent that:

- the set-off right was agreed between the parties prior to the opening of insolvency proceedings (if the set-off right was agreed after the opening of insolvency proceedings, it will only be enforceable if the relevant creditor was lawfully unaware of the opening of insolvency proceedings affecting his debtor at the time the set-off right was agreed);
- the set-off relates to mutual debts existing at the time of the opening of the insolvency proceedings; and
- such creditor is a merchant (ie, someone who regularly enters into commercial contracts).

Set-off and netting agreements will not be declared ineffective unless they constitute a gratuitous transaction (ie, a transaction for no consideration) or transaction at an undervalue, or if they have been entered into with fraudulent intent.

If the conditions set out above are not met, creditors are precluded from exercising any right of set-off following the occurrence of an insolvency event except where the claims to be set off against each other are closely connected, in which case set-off will be allowed. It is generally accepted that claims arising out of the same contract can be considered as closely connected.

The above relates to all forms of conventional set-off, that is, set-off agreed between the parties. Other forms of set-off also exist, in particular statutory set-off and judicial set-off. As set out above, statutory set-off is not enforceable after the occurrence of an insolvency event except where claims are closely connected. The right of statutory set-off of the Belgian tax authorities is enforceable after the opening of insolvency proceedings. Judicial set-off is not enforceable after the occurrence of the insolvency event.

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#### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

##### Bankruptcy

The assets of the bankrupt estate may be sold at two stages of the bankruptcy proceedings.

- The bankruptcy trustee may be authorised by the court to start selling the assets as soon as the creditors' claims are verified. Such authorisation must be general and should not single out specific assets.
- The bankruptcy trustee also has a discretionary power to sell the assets at the time of liquidation, that is, when all claims have been either rejected or accepted by the court. In such event, the court does not need either to agree on the asset sale or to supervise the implementation thereof. The court may, however, in the interest of the creditors, seek the advice of the bankrupt debtor in determining how the realisation of the assets could yield the highest proceeds.

In either case, the purchaser will acquire the assets free and clear from the insolvent estate.

##### Judicial reorganisation

During judicial reorganisation proceedings, the court can order the transfer of all or part of the business of the debtor, either with or without the debtor's consent, at the request of any interested party if the debtor is bankrupt or if an attempted reorganisation of the debtor has failed. In such circumstances, the court will appoint a representative who will manage the sale and transfer. If comparable offers are also being made, priority must be given to the preservation of employment. Once an offer has been selected, the court will hear the various stakeholders, including creditors, and will either approve, subject to conditions where appropriate, or reject the sale. Following the completion of the sale of the business, the creditors will be entitled to exercise their rights in respect of the sale proceeds and the judicial reorganisation will be terminated.

The sale of certain assets of the company can also form part of the reorganisation plan. In this case, the debtor must decide which assets it wants to sell and at what price. The reorganisation plan is then submitted to a vote and must be approved by more than half of the creditors representing more than half of the principal amount of the claims involved.

Stalking horse bids are not strictly prohibited under Belgian law, but are difficult to achieve in the context of insolvency proceedings. They would require the consent of all parties involved.

There are no overriding principles that would prohibit a creditor from bidding on its own debt. Outside a formal insolvency procedure, this will require the notary, who leads the auction process, to amend the auction rules to allow set-off. This will typically only be allowed where the debt is in excess of the amount for which security has been registered. In formal insolvency proceedings, this is much more difficult to achieve as set-off after insolvency is prohibited. Again, there would be a possibility to negotiate this with the bankruptcy trustee, but this would almost certainly require that the secured debt is in excess of the amount for which the security has been registered.

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#### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

Various pieces of IP legislation contain provisions addressing the consequences of insolvency on IP rights, with various outcomes depending on the type of IP right. In certain cases, the owner of the relevant

rights can terminate the debtor's right to use the IP upon insolvency. However, the bankruptcy trustee may also be able to continue using the relevant IP rights in certain circumstances determined by law.

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#### Personal data in insolvencies

##### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

There is no general prohibition or restriction on the transfer of personal data in a case of insolvency. That being said, such transfer is likely to fall within the scope of the Law of 8 December 1992 regarding the protection of personal data (the Data Protection Act) implementing Directive 95/46/EC.

Under the Data Protection Act, such transfer of data will amount to a communication of the data to a third party, which will become the new data controller after the transfer.

Like for any other processing of personal data, it will have to be assessed whether such transfer is justified by any of the legal grounds set out by the Data Protection Act.

If the transfer of personal data is justified by the legitimate interest of the insolvent transferor, the interests and fundamental rights of the data subjects must be taken into account. It will, thus, have to be assessed whether such legitimate interest is not overridden by the fundamental rights and freedoms of the data subjects.

In the context of customer and employee data, it may probably be argued that the transfer is also in the interest of the data subjects (as they have an interest in the continuity of the business), but this may have to be assessed with additional information on the kind of data, the purposes of the processing, etc.

In any event, it is recommended that the data subjects are informed of the transfer of the data to the third party/change of data controller. Also, if the Privacy Commission has been notified of the processing of the data that are transferred, the notification should be amended to reflect the change of data controller.

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#### Rejection and disclaimer of contracts in reorganisations

##### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

There are no specific provisions allowing the debtor to reject or disclaim an unfavourable contract. The Continuity Act, however, provides for the possibility of the debtor suspending performance of its contractual obligations if such suspension is essential for the reorganisation of the business and the counterparty is notified of the same within 14 days of the commencement of the judicial reorganisation proceedings.

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#### Arbitration processes in insolvency cases

##### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

It is generally accepted that litigation directly arising in the context of insolvency proceedings cannot be referred to arbitration. Nevertheless, leading authors have cast doubt on the validation of this general prohibition, suggesting that arbitration proceedings involving the bankruptcy trustee should be allowed, except where the courts have been granted exclusive jurisdiction over the relevant matter by law.

The court will typically allow existing arbitration proceedings to continue after insolvency proceedings are opened, although leading authors have suggested that arbitration proceedings may be suspended at the time of opening of the proceedings until the parties to the litigation have filed their claim with the bankruptcy trustee.

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#### Successful reorganisations

##### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

During the moratorium period the debtor will draft a recovery and payment plan. To be effective the plan must contain two key sections:

- a section describing the status of the company (such as the financial structure of the company, its different areas of business and their profitability, the quality and motivation of management), in addition to the difficulties it faces and how the debtor intends to resolve them; and
- a section containing the necessary measures to pay off its debts. Such measures may include deferral or reduction of principal or interest, conversion of debt to equity, the rescheduling of payments or a restricted right to set off claims. Certain secured creditors may see their payments deferred and enforcement rights suspended for up to 24 months, on the condition that they continue to be paid their interest.

The reorganisation plan is then submitted to a vote and must be approved by more than half of the creditors representing more than half of the principal amount of the claims involved. If the plan is approved and is deemed in agreement with public policy, the court will sanction the reorganisation plan and the moratorium will end. The debtor will then be required to implement and comply with the reorganisation plan and if it fails to do so, the creditors may require the court to revoke its approval of the reorganisation plan.

A reorganisation plan may also release non-debtor parties, such as sureties and guarantors from their various obligations and/or liabilities to the company's creditors.

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#### Expedited reorganisations

##### 24 Do procedures exist for expedited reorganisations?

There are no specific procedures for expedited reorganisations.

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#### Unsuccessful reorganisations

##### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A judicial reorganisation will fail if, during the moratorium, it becomes clear that the debtor can manifestly no longer preserve the continuity of its business. The court may then order the termination of the moratorium period at the request of the debtor, the public prosecutor, or any other interested party. The court will also be entitled to declare the company bankrupt or to put it into liquidation proceedings.

The reorganisation will also end if the debtor fails to file the requested documents within 14 days of its request for a judicial reorganisation or if a creditor or the public prosecutor can prove that the debtor is not carrying out the recovery plan or that a creditor or group of creditors are being unfairly prejudiced on account of the plan.

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#### Insolvency processes

##### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

Creditors are notified of the bankruptcy order by its publication in the Belgian State Gazette (upon the initiative of the clerk of the registry of the commercial court) and by its publication in two newspapers (upon the initiative of the bankruptcy trustee).

Creditors' meetings are held on several occasions during the bankruptcy process. The first creditors' meeting is held when the official verification report is delivered and the bankruptcy trustee reports on all the admitted and contested claims. The contested claims are discussed and referred to a later court session for decision on the subject matter. Further creditors' meetings may be called at any time, as the need

arises. As of the third anniversary of the declaration of bankruptcy, a creditors' meeting may be held at the request of any creditor, subject to the approval of the court (unless requested by creditors representing at least one-third of the liabilities of the bankruptcy estate, in which case the court approval is not required). At that meeting, the bankruptcy trustee explains the status of the liquidation. Finally, when the liquidation is because of finish, a creditors' meeting is held at which the final accounts are settled. Creditors' meetings are called by court order and the order is published in the Belgian State Gazette at least a month before the date of the meeting although the publication in the Belgian State Gazette can be replaced by a notice given by the bankruptcy trustee to all registered creditors.

In addition to calling meetings, creditors also have other powers in relation to the administration of the bankruptcy. Firstly, creditors may challenge the official verification report within a month of its presentation to the court. Secondly, creditors that disagree with a planned forced sale of assets during the liquidation phase may request the ad hoc appointment of a trustee for the sale. Creditors may also appeal against the court's decision regarding the final discharge of the debtor, as no action by creditors will be possible once such clearance has been given by the court. Finally, creditors have recently become entitled to file damages claims against directors of the debtor on the basis of their obvious and serious mismanagement having contributed to the bankruptcy (the law contains an irrefutable presumption that organised tax fraud within the meaning of the money laundering legislation contributes such obvious and serious mismanagement).

As set out in question 22 above, a reorganisation plan may release non-debtor parties, such as sureties and guarantors from their various obligations or liabilities or both to the company's creditors.

#### Enforcement of estate's rights

##### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

In bankruptcy proceedings, the bankruptcy trustee will have exclusive responsibility to pursue claims of the debtor. By contrast, in judicial reorganisation the debtor will continue to have the right to pursue any of its claims. It is not possible for individual creditors to pursue claims available to the estate unless the relevant creditors have the benefit of security rights over such claims that have been validly enforced.

#### Creditor representation

##### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

There is no formal process under Belgian law for the formation of creditors' committees.

#### Insolvency of corporate groups

##### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Belgian law does not formally recognise the concept of a corporate group in insolvency law and as a result, insolvency proceedings are not opened in respect of a corporate group as a whole (ie, insolvency proceedings will be opened only to the extent the conditions for the opening of insolvency proceedings are satisfied in respect of the relevant entity of the corporate group). The assets and liabilities of insolvent companies within a corporate group cannot be combined for distribution purposes, except to the extent that the individual estates of companies cannot be separately identified. For practical purposes, however, it is not uncommon for courts to hear the proceedings of entities belonging to the same corporate group simultaneously. The recast EU Insolvency Regulation of 20 May 2015 does, however, foresee new rules on the coordination of insolvency proceedings that relate to several members of the same group of companies. From 26 June 2017, any European court having jurisdiction over the insolvency proceedings

of a member of the same group of companies, may be requested by an insolvency practitioner appointed in insolvency proceedings opened in relation to a member of the group, to allow group coordination proceedings (article 61 of the recast EU Insolvency Regulation of 20 May 2015).

In general, the EU Insolvency Regulation, and the relevant provisions of Belgian domestic law, do not allow the transfer of assets from an administration in one country to an administration in another country. One exception to this is that if secondary insolvency proceedings result in a surplus, the remaining assets will be transferred to the liquidator of the main proceedings (article 35 of the EU Insolvency Regulation, upcoming article 49 of the recast EU Insolvency Regulation of 20 May 2015).

#### Appeals

##### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

The Bankruptcy Act provides for the right of appeal against a court order concerning the declaration of bankruptcy or concerning the determination of the moment upon which payments were ceased.

An appeal against the aforementioned court order has to be lodged within 15 days of the publication of the judgment in the Belgian State Gazette or from the notification of the judgment when the appeal is lodged by the bankrupt debtor.

Save for the exceptions listed in the Bankruptcy Act, any other court order made in an insolvency proceedings can also be appealed within a month of the notification of the judgment of the commercial court.

Lodging an appeal does not suspend the appealed decision during the appeal procedure.

There is no requirement to post security in order to proceed with an appeal.

#### Claims

##### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

#### Bankruptcy

All creditors must file their claims at the registrar's office of the court by the date provided for in the bankruptcy declaration (at the latest). This date is determined by the court and shall be no later than 30 days after the date of the bankruptcy order. Creditors receive notification of this requirement through its publication in the Belgian State Gazette and, to the extent their identity is known, through a letter from the bankruptcy trustee. Filing a claim requires the completion of a standard form (which contains information about the creditor, the amount of its claim and any security) and the submission of certain supporting evidence. Special provisions have also been adopted in relation to the claims filed by the employees compelling the bankruptcy trustee to assist the debtors' employees in establishing their claim.

Creditors that do not file their claim in time lose their right to participate in any distribution and lose any priority that they may have been entitled to. They can, however, still request the 'recognition' of their claims up until the day of the last creditors' meeting when all the accounts are finally settled at their own expense. If their claim is accepted at a later stage, the creditor will only be allowed to receive a portion of the assets left at that stage.

The bankruptcy order will also set the date for the final verification of claims. This date must be at least five days, and no more than 30 days, after the last date for filing claims. Claims that are disputed by the bankruptcy trustee during the verification process will be decided upon by the court after having heard the bankruptcy trustee, the debtor and the relevant creditors (to the extent they are present or represented at that meeting). The court's decision on the verification claim may be appealed in the same way as any court decision by any party to the decision.

There are no provisions specifically dealing with the transfer of claims. Any transfers would thus need to comply with the general statutory and contractual provisions on the transfer of claims. Given the filing process, it is advisable that any transfer be disclosed to the bankruptcy trustee and be filed with the court.

The creditor of a claim for contingent amounts can file such claim in an insolvency proceeding and can request that the contingent nature of the claim is taken into account. In the case of the debtor's bankruptcy, the creditor can preserve his or her rights by having the claim recorded and requesting any measures that he deems necessary (sealing assets, having an inventory made, etc). If the conditions on which the relevant claim depends would only become effective after the declaratory judgment, the bankruptcy trustee can decide to reserve the share of this creditor until such conditions are met.

It should be noted that as from the bankruptcy decision interests on unpaid amounts no longer accrue unless the creditor holds a secured or privileged claim.

#### Judicial reorganisation by way of collective agreement

In a judicial reorganisation by way of collective agreement, creditors are not required to file their claims. Instead, the debtor must draw up a list containing all claims and securities in relation to those claims and provide it to the creditors within 14 days of the moratorium period being granted. This information will then be verified by the creditors. If there is disagreement between the creditor and the debtor, the courts will resolve such a dispute.

#### Modifying creditors' rights

##### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

A court cannot change the rank of a creditor's claim in a bankruptcy, as such ranking is determined by law. In a judicial reorganisation, a court may approve a restructuring plan that modifies the ranking of a class of claims.

#### Priority claims

##### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

#### Government priority claims

The most important government statutory liens are those asserted by the social security and tax authorities (including direct and indirect taxes, national, regional and local taxes). However, these do not rank higher than the claims of secured creditors and certain other specific statutory liens also take precedence, including the following non-government priority claims:

- enforcement costs incurred in the interest of creditors generally;
- costs incurred in saving or maintaining a specific asset;
- the unpaid purchase price for the sale of moveable or immovable assets;
- unpaid rent on a building; and
- unpaid premiums for the insurance of assets.

The bankruptcy legislation distinguishes between general statutory liens, which apply in general to the bankrupt estate, and specific statutory liens, which apply to specific assets within the bankrupt estate. As a general rule, specific statutory liens will take priority over general statutory liens. Priority among specific statutory liens will be determined by the law, which establishes a ranking of these specific statutory liens. Secured claims will, in general, take priority over any general statutory liens. Priority between creditors with a specific statutory lien and secured creditors has generated a substantial amount of case law, where often the date on which the security interest has become enforceable against third parties will determine priority.

It should be noted that administrative expenses will take priority over unsecured creditors and creditors with a general statutory lien. They will also take priority over secured creditors and creditors with a specific statutory lien, but only to the extent that they have benefited from the administrative expenses.

#### Employment-related liabilities in restructurings

##### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

A restructuring involving a substantial reduction of the workforce may, depending on the number of proposed dismissals and the time frame during which these dismissals are to be made, constitute a collective dismissal. Where this is the case, specific obligations are imposed on the employer in addition to the usual statutory requirements relating to the termination of individual contracts, including a requirement to provide significant prior information to, and to continue to consult with, the employee representatives or the employees themselves, and to notify the labour authorities before any final decision is taken. Furthermore, a collective dismissal also triggers specific employment-related measures such as the payment of a specific collective dismissal or closure indemnity to the dismissed employees (on top of their standard severance package) and the setting up of an outplacement service, etc.

In a restructuring involving bankruptcy proceedings, claims of employees against the employer will essentially relate to the payment of unpaid severance entitlements following the termination of their employment contracts and their pension entitlements. In the case of a reorganisation under the Continuity Act, the reorganisation plan cannot reduce the payments related to employment contracts for services provided prior to the reorganisation.

With respect to pension liabilities in cases where occupational pension plans have been set up by the employer for the benefit of the employees, the main protection against employer insolvency is the external financing requirement for occupational pension schemes (see question 35). As a consequence, employer insolvency must not be detrimental to an employee's occupational complementary pension entitlements.

Where an employer has not funded an occupational pension plan sufficiently, an employee's pension entitlements under that plan may be reduced and the Belgian Business Closure Fund may intervene. Employees can file a claim against the insolvent employer in respect of the loss suffered as a consequence of such underfunding.

Claims for unpaid severance entitlements, have priority in proceedings against an insolvent employer. However, this priority relates only to the proceeds of the employer's moveable assets.

#### Pension claims

##### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

In Belgium, pension arrangements are externalised (eg, with an insurance company) or held by a different entity than the employer (eg, a pension fund). A bankruptcy of the employer will not have any influence on the rights that are already accumulated under the relevant pension arrangement. Acquired reserves are absolutely protected. There is, however, no priority attached to a claim of pension benefit.

Employees benefit from a priority right with respect to unpaid wages, but the question whether such priority right should also be attached to a claim of the employee concerning the unpaid contribution by the employer is unsettled in case law.

Similarly, there is no complete consensus on whether the Belgian Business Closure Fund should intervene to cover the unpaid employer's contributions in the event of closure of the business. In any event, the Belgian Business Closure Fund's intervention would be capped.

#### Environmental problems and liabilities

##### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Environmental liability of an insolvent party will be treated like all other unsecured liabilities. It should be noted that particular liabilities and obligations may be imposed through specific legislation. For instance, under the decree of the Flemish Council of 27 October 2006 concerning soil decontamination and soil protection, the curator in insolvency

proceedings has the obligation to issue a soil examination for terrain owned by the company and that is prone to particular risks.

### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

The liabilities of a debtor will survive insolvency, except where a natural person (ie, not a company or other corporate entity) has been formally discharged by the court. Technically, creditors will regain their rights against a corporate debtor following the completion of insolvency proceedings; however, if the debtor is a company the decision of the court to close the insolvency proceedings entails the automatic dissolution and liquidation of the company. This means that, in practice, liabilities do not survive insolvency.

The liabilities of a debtor will typically not be enforceable against a purchaser of the debtor's assets in insolvency. There are a number of important exceptions to this principle:

- in accepting the transfer of parts of a business in a going concern, the court may impose certain conditions, including the transfer of certain liabilities to the purchaser of the relevant assets; and
- in certain cases, liabilities specifically linked with the transferred assets may transfer as well as a direct consequence of their close connection with the relevant asset.

### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Distributions are made on a *pari passu* basis with the exception of administration expenses and creditors benefiting from a security interest or a specific statutory lien.

The costs, debts and expenses incurred in the management of the estate will be paid out first. Creditors enjoying a security interest or a specific statutory lien (as opposed to a general statutory lien) are then entitled to be paid out of the proceeds of the sale of the secured assets. If the proceeds of the sale of the secured assets are insufficient to pay the secured creditors, or holders of a specific statutory lien, then those creditors may be admitted as unsecured creditors for the remainder of their claims, provided their claims have been properly declared and verified.

Distributions can be made as soon as the bankruptcy trustee has verified all claims filed. Hence, the trustee will not have to wait until the closing of the bankruptcy. The bankruptcy trustee may start selling assets even earlier, that is, as soon as he or she considers that maintenance costs are too high.

Distributions in reorganisations are generally made in accordance with the repayment and recovery plan or the amicable settlement agreement.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

All arrangements, transfers and payments made by the bankrupt debtor after the declaration of bankruptcy are void.

Moreover, any transaction or payment effected with fraudulent intent may be set aside irrespective of when it was entered into. If a transaction is set aside, the proceeds from it must be returned to the bankrupt's estate. The bankrupt's estate can also be required to return any money or assets it received under the transaction to the relevant creditor. However, in most cases the creditor's claim for restitution or repayment will form an unsecured claim in the bankruptcy.

See also question 38.

There are no provisions specifically dealing with the annulment of transactions in reorganisations.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

As a principle, the date on which the debtor is considered insolvent (ie, has ceased to pay his or her debts in a persistent manner) is that of the bankruptcy order. However, in certain circumstances, the court can fix a period of a maximum of six months before the opening of the insolvency proceedings in which the debtor is assumed to have already been insolvent: this will be the 'suspect period'. The following transactions are *per se* void when entered into during the suspect period:

- any transaction where the value given by the company significantly exceeds the value it received as consideration;
- any payments of debt that was not yet due (as well as all payments other than with money or equivalent financial instruments); and
- any security granted during the suspect period in relation to a debt that existed prior to the date on which the security was granted.

Furthermore, any transaction entered into by a company that has ceased paying its debts may be avoided upon the subsequent bankruptcy of the company if the counterparty to the transaction was aware of the cessation of payments.

Voidable transactions may only be attacked by the bankruptcy trustee as from the date of the bankruptcy.

It should be noted that the Belgian Supreme Court held, in a decision dated 10 January 2003, that when a judicial composition order is followed by a bankruptcy order, the commercial court is entitled to fix the starting point of the cessation of payment or suspect period on the date of the request for judicial composition (despite the fact that the judicial composition order is supposed to be granted only when the debtor is 'temporarily' unable to pay its debts whereas the cessation of payment means that the debtor has ceased to pay his or her debts in a persistent manner – see above).

The rules relating to the suspect period will in certain circumstances be disappplied to the extent that they relate to set-off arrangements (and payments made in respect thereof) or to the creation of pledges pursuant to the Financial Collateral Act. These transactions will therefore not be capable of being avoided.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

In general, directors and officers are not liable for the company's debts. There are, however, in addition to the normal rules on directors' liability (in particular for breaches of the company's charter or the legislation on corporations), certain specific provisions applicable in relation to bankruptcy. Accordingly, directors or former directors of a bankrupt company may be held liable at the initiative of the bankruptcy trustee or of the creditors if, owing to their obvious and serious mismanagement, the company is unable to pay its debts in full. In such case, the directors will be liable to the extent that the creditors are not fully satisfied out of the proceeds. In addition, specific legislation allows the tax and social security administration, as well as the bankruptcy trustee, to hold directors of certain companies liable for certain amounts due in respect of compliance with tax and social security legislation.

In addition to the liabilities described above, directors may be held liable (both from a civil and criminal perspective) if they fail to file for bankruptcy in a timely fashion. If a court finds that an obvious and serious mismanagement by a director has contributed to the company becoming bankrupt, it may bar that director from being a director or other officer of any company for three to 10 years.

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**Groups of companies**
**42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

Insolvency proceedings are organised per legal entity. 'Piercing the corporate veil' is very exceptional in Belgium. It would only occur in the event that there is a commingling of assets and liabilities of different entities (eg, no separate accounting and cross-payments of liabilities without a legal framework) or in fraudulent transactions in which several entities took part.

If a parent company is also a director (as a legal entity) of one of its subsidiaries, it could become liable as a director of that subsidiary in the event of, for example, mismanagement or breaches of law committed as a director of the subsidiary and, as a result, become liable for its debts.

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**Insider claims**
**43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

There is no specific rule in this respect. In the case of a non-arm's length transaction, it could, however, be argued that the transaction has been concluded outside the corporate interest of the potential bankrupt company and as a result is unenforceable.

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**Creditors' enforcement**
**44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

There are no general processes in Belgian law by which some or all of the assets of a business can be seized outside court proceedings.

The Financial Collateral Law provides for the possibility for the pledgee to appropriate or sell pledged financial collateral outside court proceedings.

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**Corporate procedures**
**45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

Belgian company law provides for voluntary dissolution and liquidation. Involuntary dissolution and liquidation may be ordered by the commercial court in the following cases:

- at the initiative of any interested party or of the public prosecutor if the company has failed to file its accounts for three consecutive financial years;
- at the initiative of any interested party if the net assets of the company drop below €61,500, which corresponds to the minimum share capital of a public company with limited liability; or
- at the initiative of any shareholder (or of any interested party, according to some legal writers) when there are just causes, for example, in the case of heavy losses, repeated irregularities or abuse of majority voting.

In all these cases, liquidators are obliged to pay out to the creditors in accordance with the principle of equal treatment, subject, however, to the rights of secured creditors or creditors benefiting from a specific statutory lien. This process has a great degree of similarity with bankruptcy proceedings, with the exception that the court is not, in principle at least, involved in the liquidation proceedings, which are held on an informal basis.

In addition, it should be noted that a corporation that has been dissolved and is in the process of being liquidated can still be declared bankrupt, to the extent that the conditions for bankruptcy are met.

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**Conclusion of case**
**46 How are liquidation and reorganisation cases formally concluded?**
**Voluntary or involuntary liquidation other than bankruptcy**

Where a company has been liquidated either voluntarily or involuntarily, the liquidation will end with a distribution to the shareholders of

all the assets that remain after debts have been paid or provided for. The liquidators will call a general meeting of shareholders to which the liquidators submit the final accounts and at which the shareholders appoint commissioners to review the accounts. At a second general meeting, the shareholders review the way the liquidators have performed their duties based on a report presented by the commissioners. The formal termination of the liquidation will be published in the Belgian State Gazette and filed in the company's official record at the commercial court.

**Conclusion of bankruptcy liquidation**

A bankruptcy may be terminated by the court (ex officio or at the initiative of the bankruptcy trustee) summarily when it is established that the assets will not cover the expenses of management and liquidation of the bankrupt estate. The judgment ordering the termination will be published in the Belgian State Gazette. As a consequence of that decision, the bankrupt company will be immediately dissolved.

Termination of the bankruptcy after a full liquidation of the assets is only ordered by the court at the request of the bankruptcy trustee. The bankruptcy trustee will make the request following a final creditors' meeting where the final accounts of the liquidation are presented and discussed, and after the final distribution of the liquidation proceeds. The debtor will be notified of the trustee's application by the court and will have the opportunity to oppose the closure. The termination order will only come into force one month after its publication, during which time the court may withdraw the order at the request of the creditors.

A bankrupt individual (as opposed to a company) having acted in good faith, as well as a physical person who guaranteed the debts of the debtor free of charge, will in principle be discharged from any remaining debts.

The termination order relating to the bankruptcy of a company will cause the immediate dissolution of the company. The order will be published by the clerk of the registry of the commercial court in the Belgian State Gazette.

As the discharge cancels the remaining debts of the bankrupt debtor, the guarantor will thus no longer be subrogated to the rights of the creditor to the extent that the latter called on the guarantee prior to the bankruptcy, nor will the guarantor be able to hold against the creditor the exceptions available to the debtor relating to the debt.

**Conclusion of a judicial reorganisation**

A judicial reorganisation is concluded by:

- the court concluding that the debtor can manifestly no longer assure the continuity of its business (ie, that the debtor is unable to enter into an amicable settlement or a collective agreement with its creditors);
- an agreed amicable settlement presented to the court;
- the full performance of the reorganisation plan;
- the revocation of the reorganisation plan by the court;
- the completion of the sale of the business; and
- a declaration of bankruptcy or liquidation.

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**International cases**
**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Since 31 May 2002, the provisions applicable to cross-border insolvency proceedings have differed depending on whether or not they are covered by Council Regulation (EC) No. 1346/2000 on insolvency proceedings (the EU Insolvency Regulation). This Regulation will be replaced by Regulation (EU) 2015/848 of the European Parliament and Council of 20 May 2015 on insolvency proceedings (entry into force: 26 June 2017).

### Within the scope of the EU Insolvency Regulation

The EU Insolvency Regulation sets out harmonised rules on conflict of laws and jurisdiction applying to intra-EU collective insolvency proceedings. The regulation specifies in annex A the relevant insolvency proceedings to which it applies in each member state (other than Denmark), which for Belgium are bankruptcy, judicial reorganisation and matters relating to private individuals' collective debt rescheduling (EU insolvency proceedings). With respect to Belgium, other types of Belgian insolvency procedures bringing about mandatory *pari passu* ranking of unsecured creditors (such as voluntary or judicial winding-up or attachment proceedings under the Belgian Judicial Code) thus fall outside its scope.

Debtors that are credit institutions, insurance undertakings, investment undertakings that provide services involving the holding of funds or securities for third parties, or collective investment undertakings are specifically excluded from the regulation.

Under the EU Insolvency Regulation, if the debtor has interests in several member states but the centre of his main interests is located in Belgium, Belgian courts will have jurisdiction to open EU insolvency proceedings in respect of such debtor. These proceedings are, with respect to other member states, universal in scope, governed by Belgian law (*lex concursus*) and are, in principle, effective in all member states. Likewise, when the centre of main interests of a debtor is located outside Belgium, such other jurisdiction and *lex concursus* will in principle be effective in Belgium. The applicable law determines all the effects of the EU insolvency proceedings, both procedural and substantive. It governs all the conditions for the opening, conduct and closure of the proceedings. The 'centre of main interests' corresponds to the place where the debtor conducts the administration of his or her interests on a regular basis. In the case of companies, the place of the registered office of such company is presumed to be the centre of the company's main interests in the absence of proof to the contrary.

Even if the centre of a debtor's main interests is in Belgium (or another member state), the courts of another member state (or Belgium) may open secondary proceedings in the event that such debtor possesses an establishment (being any place of operations where the debtor carries out a non-transitory economic activity with human goods and means) in the territory of such other member state (or Belgium). The secondary proceedings are to be governed by the applicable law of that other member state (or Belgium). However, secondary proceedings are territorial in scope and so will not extend beyond the member state where they are opened, save in respect of creditors who have given their consent.

With respect to Belgium, the EU Insolvency Regulation will, in the context of EU insolvency proceedings, supersede those Belgian national rules and treaties on conflict of laws and jurisdiction to the extent of the matters covered in the regulation (see below).

### Outside the scope of the EU Insolvency Regulation

#### *National conflict rules - Private International Law Code*

Except as set out further below, situations not covered by the EU Insolvency Regulation are governed by the Belgian Private International Law Code. The provisions of the Code containing the conflict of laws rules relating to insolvency proceedings follow, to a large extent, the rules set out in the EU Insolvency Regulation. This means that:

- insolvency proceedings falling under the Code are those existing under Belgian law (bankruptcy, judicial reorganisation and collective debt rescheduling) but also foreign proceedings based on a debtor's collective insolvency; and
- insolvency proceedings can be principal proceedings (ie, universal proceedings having effect on all the debtor's assets) or territorial (secondary) proceedings (ie, having effects limited to the debtor's assets located within the territory of the state where the proceedings are opened).

As to the criterion of jurisdiction allowing Belgian courts to open insolvency proceedings, the Code provides that main proceedings may be opened in Belgium when:

- the principal establishment of the debtor is in Belgium - one should note in this respect that the notion of principal establishment is similar (although not exactly identical) to the concept of 'centre of main interest' in the EU Insolvency Regulation; or

- the registered office of the company is in Belgium (which is an additional connecting factor by comparison with the EU Insolvency Regulation).

The Code also upholds the jurisdiction of the Belgian courts to open territorial proceedings when the debtor has an establishment in Belgium (and principal establishment or centre of main interest outside the territory of the European Union).

Moreover, the Code provides for an automatic recognition of certain foreign decisions on insolvency. Execution requires an *exequatur*, a condition also required by the EU Insolvency Regulation.

### *Insolvency treaties*

Belgium has entered into bilateral insolvency treaties with Austria, France and the Netherlands. The scope of application of such insolvency treaties has become very limited following the entry into force of the EU Insolvency Regulation on 31 May 2002 and the legislative changes relating to the reorganisation and winding up of credit institutions and insurance undertakings by the Law of 6 December 2004. The bilateral treaties only apply with respect to matters that are not covered by the EU Insolvency Regulation and with respect to entities that are not covered by either the EU Insolvency Regulation or the EU directives on the reorganisation and winding up of credit institutions and insurance undertakings.

### *EEX*

While the EEX Treaty (which for the EU member states has been effectively replaced by the Brussels Ibis Regulation No. 1215/2012 of 12 December 2012) in principle does not apply to insolvency proceedings, it may nevertheless cover situations that are connected to insolvency proceedings (eg, out-of-court settlements and claims for compensation by the bankruptcy trustee against the purchaser of assets sold by the debtor in the suspect period). In such event, there may be a divergence between the applicable jurisdiction and enforcement rules for aspects covered by the EU Insolvency Regulation and others covered by the EEX Treaty. This may lead to possible parallel proceedings in several jurisdictions that are not subject to coordination and mutual information rules, similar to those applying between principal and secondary proceedings in the context of the EU Insolvency Regulation.

There are currently no plans to adopt the UNCITRAL Model Law on Cross-Border Insolvency into Belgian law.

### **COMI**

#### **48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

When the legislator used COMI, he was mindful of the European definition used in the insolvency regulations. In addition, the parliamentary works indicate that there will normally be a large overlap between the terms 'centre of main interests' and 'principal place of business'. As such, the registered office of a company is not necessarily its principal place of business or COMI. In a recent case, the commercial court of Bruges took into account the location of the board meetings, the nationality of the directors and the fact that the day-to-day management was handled by a Belgian company to hold that a Luxembourg-incorporated entity had its centre of main interests in Belgium.

As indicated above, Belgian law does not use the concept of group companies. Therefore, the determination of the centre of main interests of group companies is not relevant.

### **Cross-border cooperation**

#### **49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

The Belgian Private International Law Code states that decision of foreign insolvency proceedings, not falling within the scope of the

European insolvency regulations, may be recognised and executed in Belgium. The competent courts for the recognition of foreign insolvency proceedings are the commercial courts, with an exception for proceedings for insolvent individuals, for which the courts of first instance are competent. The courts will only recognise foreign decisions if certain conditions are met, such as the compatibility with Belgian public order, the rights of defence were respected and recognition relates to a final decision.

The Private International Law Code also imposes a general obligation of cooperation on the bankruptcy trustee of the main or territorial proceedings opened in Belgium with the administrator of the foreign proceedings, subject to a condition of reciprocity and only in so far as the costs of such cooperation are not excessive, taking into account the debtor's assets.

Although not prohibited under Belgian law, the instances in which Belgian courts have entered into communications with foreign courts in cross-border insolvencies and restructurings have been very limited. Such communication was attempted in the framework of the bankruptcy of Lernout & Hauspie Speech Products NV (L&H). At the end of 2000, L&H obtained bankruptcy protection under Chapter 11 of the US Bankruptcy Code. At the same time, L&H filed a request for judicial composition in Belgium. In this framework, Stonington Partners Inc made a claim resulting from securities fraud. Under US law, this claim would have been subordinated to other claims and would thus effectively not have received any share in the bankruptcy estate. Under

Belgian law, the claim (if proven) would have ranked on par with all other unsecured claims. At first instance, the relevant US court decided to apply US law. The Court of Appeal remanded this decision and made a 'strong recommendation' to the bankruptcy judge to enter into direct communication with the Belgian bankruptcy trustees and the Belgian court. The lower court, however, refused to follow this recommendation and no actual communication between the Belgian and US courts was made.

We are not aware of any courts that have refused to recognise foreign proceedings or to cooperate with foreign courts.

#### **Cross-border insolvency protocols and joint court hearings**

**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

There are no official cross-border insolvency protocols (or other similar arrangements) between Belgian courts and courts in other countries.

The occasions in which Belgian courts have communicated with courts in other countries in cross-border insolvency proceedings have been very limited. The best-known attempt to establish such communication was made in the framework of the L&H insolvency (see question 47).



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# Bermuda

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Companies Act 1981 governs insolvencies and reorganisations in Bermuda. The solvency tests include a 'cash-flow' test requiring a company to be able to pay its undisputed liabilities as they fall due and a 'balance-sheet' test requiring a company's assets to exceed its liabilities. An unsatisfied judgment or statutory demand in respect of an undisputed debt exceeding 500 Bermuda dollars will justify the making of a winding-up order at the instance of a creditor. Prospective or contingent creditors may petition on giving security and showing a prima facie case that the company is insolvent. The insolvency regime of Companies Act 1981 is based largely on the English Companies Act 1948, with some minor modifications.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The Supreme Court of Bermuda is the court of superior record with unlimited jurisdiction over insolvencies and reorganisations.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The Bankruptcy Act 1989 applies to personal insolvencies. Assets that have been validly assigned or charged to secure indebtedness are excluded from the insolvency proceeding (unless the security is surrendered) and assets that are held in trust by the insolvent are excluded from the estate. Licensed banks are to be governed by a separate insolvency regime established under the Banks (Special Resolution Regime) Act 2016, which has been passed but has not yet been brought into effect.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There are no specific procedures that apply to government-owned enterprises, and in the case of a statutory corporation, or quango, or other entity that has legal personality, it can be sued in the normal way. It is an implied principle of public law that a government-owned entity will honour its obligations, and there are no cases in which the court has had to consider the possibility of winding up a government-owned entity.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No. The Banks (Special Resolution Regime) Act 2016 creates a mechanism for the rescue and sale of licensed banks, but this regime does not provide for the insulation of banks from insolvency.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

Legal mortgages and equitable mortgages by deposits of title deeds are the most usual types of security taken on real property.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

Fixed and floating charges, debentures, chattel mortgages, liens, pledges and retention of title clauses by contract are all available as security over personal property.

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## Unsecured credit

### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

A judgment creditor may examine a judgment debtor upon his or her means to pay the debt and the court may make instalment orders, remedied by orders of contempt in default. Principally, the means of enforcement of judgments are writs of execution, writs of possession and garnishee proceedings. Pre-judgment attachment is not available, although injunction relief pending judgment is available in appropriate circumstances. A judgment attaches to the real property owned by a judgment debtor until payment. Foreign creditors may have to provide security for costs when commencing an action to recover a debt from a Bermuda entity or person.

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## Voluntary liquidations

### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Members' voluntary liquidations are solvent liquidations and are not conducted under the supervision of the court, and no formal liquidation proceeding is required. A members' voluntary liquidation must be concluded within 12 months of its commencement. Once appointed, the liquidator has full control of the liquidation and the directors' powers cease.

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## Involuntary liquidations

### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

A company that is insolvent (ie, cash-flow or balance-sheet insolvent) must cease trading and commence a liquidation proceeding. A

creditor can present a winding-up petition based on the insolvency of the company. Prospective and contingent creditors must prove a prima facie case for winding up and provide security for costs. Policyholders of insurance companies with solely contingent claims are under some restrictions in their ability to commence involuntary liquidation proceedings.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

A voluntary reorganisation can be achieved by a scheme of arrangement between the company and its creditors or members (or any class of them) if the arrangement is approved by a majority in number and three-quarters in value of each class voting on the scheme.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Creditors may seek to invoke the liquidators' support in a scheme of arrangement, but otherwise cannot commence an involuntary reorganisation. A liquidator has power to sell the whole (or part) of the undertaking of the company under section 101 of the Companies Act in conjunction with an approved scheme of arrangement.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Directors must not allow a company to continue to trade when the company is insolvent and may incur personal liability for debts incurred if it continues to trade while insolvent. Directors are not obliged to commence insolvency proceedings, but will usually either resign or file a petition on behalf of the company if a creditor does not do so. Directors' liabilities are often limited under the by-laws of the company to exonerate them from liability except for personal fraud or dishonesty.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

In provisional liquidation, the provisional liquidator (or the directors if authorised by the court) may continue to carry on business during a reorganisation. Expenses incurred by the liquidator as expenses of the liquidation will be treated as preferred claims and court authorisation is required to meet new obligations incurred after a filing out of the assets of the company and in priority to other unsecured creditors. Directors can continue to operate the company and manage its affairs until a winding-up order is made, after which directors' powers cease. Directors have residual powers to appeal against the making of a winding-up order on behalf of the company. After a provisional liquidator is appointed, the directors' powers cease but in certain cases they may be allowed to continue to manage the company subject to limitations set out in the order of appointment of the provisional liquidator (eg, as in a 'soft touch' provisional liquidation).

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

Upon the appointment of a provisional liquidator, or the making of a winding-up order, there is an automatic stay of all proceedings by or against the company, unless the court orders otherwise.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Generally not. In cases where a funding agreement has been approved by the court, a creditor funding necessary liquidation expenses may be granted priority over unsecured creditors to the extent of the additional credit provided or expenses incurred in the liquidation.

### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Automatic set-off applies upon the making of a compulsory winding up order. Creditors cannot be deprived of mandatory set-off.

### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

Generally, a liquidator can sell specific assets in the ordinary course of business, usually with the sanction of the court or the committee of inspection. Assets purchased from a liquidator in these circumstances are 'free and clear'. Creditors can bid in sales and stalking horse bids are permissible. The court will take into account the fairness of the bid, and may require a fairness opinion or valuation to support the bid. This applies where the credit bidder is the original creditor or an assignee, subject to the general public policy restrictions on creditors trafficking in debt.

### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

Generally, an IP licensor cannot terminate the debtor's right to use it unless this is a specific term of the licensing agreement and, if so, the liquidator can negotiate terms of use after insolvency.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Personal Information Protection Act 2016 requires that the personal information gathered must be kept confidential and may only be used with the person's consent. A Code of Practice will be implemented to set out best practices for the protection of and use of personal information. The Act has been passed but has not been brought into force, and no Code of Practice has been published.

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**Rejection and disclaimer of contracts in reorganisations**

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

A permanent liquidator may disclaim an onerous contract or one that is unprofitable or unsaleable and the disclaimer operates from the date of service of notice disclaiming the contract, following the grant of leave to disclaim by the court. The court may also make a vesting order or award compensation to the party whose contract has been disclaimed. If the debtor company breaches a contract after the filing of a petition, a claim for breach of contract may still be made provided that the damages can be the subject of a liquidated claim. Usually a liquidator is appointed within a short period after the filing of the petition for compulsory winding up, and the making of a winding-up order will have the effect of terminating the contract.

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**Arbitration processes in insolvency cases**

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Generally, a liquidator will be subject to the same rights and restrictions as the company was subject, including its contractual rights of arbitration. However, creditors with disputed proofs of debt are required to appeal against a rejected proof of debt, irrespective of arbitration. Where no liquidated or quantified liability is established, then an arbitration clause will operate normally, subject to the leave of the court to prosecute the claim against the company being given to the creditor. The court does not mandate arbitration but will allow it where the parties agree to it. Insolvency disputes (ie, those arising out of the conduct of the liquidation as a result of the liquidator's appointment) are not arbitrated but are dealt with by the court exercising its powers of supervision over the liquidation.

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**Successful reorganisations**

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

Creditors must be separated into classes with similar interest so that they can reasonably consult and vote on a resolution in favour or against a proposal for reorganisation. Classes are determined as a preliminary step in the proposal for a scheme and the initial order to convene the relevant meetings to consider the plan of reorganisation by a scheme of arrangement.

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**Expedited reorganisations**

- 24 Do procedures exist for expedited reorganisations?**

There are no pre-packaged reorganisation provisions in the Companies Act.

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**Unsuccessful reorganisations**

- 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

The ordinary winding-up process will continue if the reorganisation proposal is not carried by the necessary majorities (ie, a majority number and three-quarters in value) and the sanction of the court to the scheme.

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**Insolvency processes**

- 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

The first meeting of creditors is convened to approve the appointment of a permanent liquidator and (if approved) a committee of inspection at an early stage. Thereafter, there are annual meetings and reports and special meetings may be called to consider extraordinary business. The information usually available to creditors are the total assets and total liabilities of the estate and the formal report to the court. Members of the creditors' committee will usually have access to greater information but will be restricted as to its use. Generally, creditors cannot pursue independent claims against third parties, but (subject to restrictions in the by-laws) may make claims of misfeasance on the part of directors (although this is rarely if ever done) and may make claims against former officers for fraudulent trading. A reorganisation plan cannot provide for the release of liabilities owed by third parties who are not otherwise also subject to a scheme of arrangement that makes provision for the compromise of those claims, and is subject to appropriate safeguards approved by the court for the rights of dissenting creditors.

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**Enforcement of estate's rights**

- 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

Generally not. In principle it is possible to assign a claim of the company to a creditor for value or to enter a funding agreement to enable a claim to be pursued in right of the company subject to payment of expenses in priority, but the proceeds of the successful claim enure to the whole estate after payment of expenses to the funding creditor.

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**Creditor representation**

- 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

The committee of inspection can sanction the liquidator taking actions to further the administration of the liquidation and prosecute claims, sell assets and make compromises. The committee has no independent powers and will usually audit the receipts and payments of the liquidator and submit an await report to the court. Members of the committee are unpaid (except for reimbursement of expenses). Members are appointed by resolution of the creditors and contributories at the first meeting, and are then approved by the court.

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**Insolvency of corporate groups**

- 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

No. Only in extreme circumstances can the court 'pool' assets of a group, that is, only where it is impossible to determine which asset belongs to which company. The juridical basis for the approach is unreliable and it is not generally possible to disregard the formal independent legal personality of group companies.

## Appeals

- 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

There is a right of appeal from a final order made by a court in an insolvency proceeding. This right can be exercised only by a party to the proceeding. Where the order is an interlocutory order, permission to appeal must be sought from the Supreme Court and if refused may be sought from the Court of Appeal. Security for costs will usually be required on an appeal from a final order, or if leave is granted, from an interlocutory order, in accordance with an assessment of the likely costs of the prosecution of the appeal and the preparation of the record for the appeal, and must be posted or secured prior to the hearing of the appeal in accordance with the directions given for the appeal by the Registrar of the Court of Appeal.

## Claims

- 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

A creditor must lodge a proof of debt within the time stated by the liquidator. If disallowed, a creditor must appeal to the court within 21 days of receiving the notice of rejection. Creditors must usually value their contingent unliquidated claims at a present day value and support the valuation by evidence. A claim in a liquidation may be assigned, and can be the subject of a proof of debt for the full amount. However, there are public policy restrictions that prevent creditors from 'trafficking' in debt (eg, to obtain the benefit of mandatory set-off relief).

## Modifying creditors' rights

- 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

There is no power to change an unsecured creditor's claim as to priority, except for post-liquidation claims for expenses or services rendered to the liquidator, which will rank ahead of preferred claims.

## Priority claims

- 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Secured creditors have priority (as their claims fall outside the liquidation process). Government taxes, workers' compensation liabilities, pension contributions and employee wages are the principal categories of preferred claims.

## Employment-related liabilities in restructurings

- 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

Termination of employment may give rise to claims for compensation or redundancy payment, or both, under the Employment Act 2000, but the value of these claims is limited to a claim not exceeding 2,500 Bermuda dollars per employee, unless the terms of employment provide for a lump sum or gratuity at the end of employment, where the full amount is recoverable, assuming there are assets with which to pay it. Redundancy and severance claims are treated as unsecured claims with no priority, but are treated as preferential claims, and redundancy payments are limited to 26 weeks' pay. The winding up of the company will cause the contract of employment to terminate automatically one month from the date of the winding-up order.

## Update and trends

The jurisdiction is reviewing the need for an updated procedure for winding up companies, and amending the law to make special provision for the recognition of foreign office holders. It is unlikely that Bermuda will adopt the UNCITRAL model law on cross-border insolvency at this time. The Bank (Special Resolution Regime) Act 2016 will require the introduction of special rules for the administration and implementation of a bank insolvency proceeding.

## Pension claims

- 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Generally, there are no claims available against employers for actuarial deficiencies and in the majority of cases, pensions are contributory schemes. Directors may be personally liable for employment taxes deducted but not paid in respect of an employee's account.

## Environmental problems and liabilities

- 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

There are no special rules for environmental problems or liabilities under Bermuda law.

## Liabilities that survive insolvency proceedings

- 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

Generally not, but only where specifically provided in the plan of reorganisation. In the case of personal bankruptcies, awards of damages against a bankrupt are not discharged on the discharge of a bankrupt.

## Distributions

- 38 How and when are distributions made to creditors in liquidations and reorganisations?**

The liquidator may make interim dividends at any time to those creditors whose proofs of debt have been admitted to proof and will make a final dividend once all assets have been collected.

## Transactions that may be annulled

- 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Fraudulent conveyances and transactions at an undervalue within six years, floating charges within one year and voidable preferences within six months of the commencement of the liquidation can be annulled or set aside in liquidations and reorganisations.

## Proceedings to annul transactions

- 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

A floating charge may be set aside within one year if the company was not solvent at the time it was granted and payments with intent to prefer one or more creditors over others made within six months of the liquidation may be recovered from the payee.

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**Directors and officers**

- 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

Directors may be liable for employment tax not paid in respect of an employee of the company.

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**Groups of companies**

- 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

Generally this is not possible. A court is not able to order a distribution of assets pro rata without regard to the rules of separate corporate personality, in the absence of a scheme of arrangement which is binding on all members of the group.

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**Insider claims**

- 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

There is no concept of a 'non-arm's length creditor', but creditors who are related to the debtor may have more difficulty defending claims for voidable preference within six months of the liquidation.

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**Creditors' enforcement**

- 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

No. Secured assets do not fall within the estate.

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**Corporate procedures**

- 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

The rules for personal bankruptcy differ in a number of respects, but the rules for the admission or proofs, priority of claims, contingent and future claims are the same.

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**Conclusion of case**

- 46 How are liquidation and reorganisation cases formally concluded?**

The liquidator will convene a final meeting, lay the accounts for approval by the creditors, make the final dividend and seek a release from the court.

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**International cases**

- 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Foreign liquidators are normally recognised in Bermuda and where assets exist in Bermuda belonging to a foreign company in liquidation, an ancillary proceeding may be commenced in Bermuda. Recognition of foreign judgment is limited to the United Kingdom and certain named Commonwealth jurisdictions. The UNCITRAL Model Law on Cross-Border Insolvency has not been adopted in Bermuda.

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**COMI**

- 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

There are no special rules to determine COMI. If the debtor is registered in Bermuda, or has a place of business in Bermuda, or has assets within Bermuda, the court may exercise its jurisdiction to wind up the company's affairs in Bermuda.

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**Cross-border cooperation**

- 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

Generally, the Bermuda court will assist foreign liquidators where possible, but usually an ancillary liquidation proceeding will be required in Bermuda if substantive legal action has to be taken within the jurisdiction by a foreign liquidator. The Privy Council has ruled that although a Bermuda court has power to recognise the request of foreign liquidators, the power to give assistance is limited by the scope of the court's own powers under the Companies Act, or its common law powers. The scope of the extent to which common law powers can be used to assist a foreign liquidator is still developing.



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**Cross-border insolvency protocols and joint court hearings**

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- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

No, there is no official protocol. Insolvency judges may, with the consent of parties, liaise with insolvency judges in foreign jurisdictions, to coordinate the making of orders in their respective jurisdictions in relation to an insolvency common to both jurisdictions, but this is limited in practice.

# Botswana

Kwadwo Osei-Ofei\*

Osei-Ofei Swabi & Co

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## Legislation

- 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?**

The legislation applicable to bankruptcies and reorganisations in Botswana is the Insolvency Act and the Companies Act. An entity is insolvent if it is unable to liquidate debts as and when they fall due for payment.

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## Courts

- 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?**

The High Court has unlimited jurisdiction in all civil matters and is the court where petitions for liquidation must be presented.

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## Excluded entities and excluded assets

- 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?**

Sections 20 and 27 of the Insolvency Act exclude certain assets that may be deemed to belong to the spouse and were acquired prior to the marriage and certain life insurance policies up to a set amount ceded to a spouse.

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## Public enterprises

- 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?**

The Insolvency Act applies to all entities whether private or public and same procedures apply.

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## Protection for large financial institutions

- 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?**

We are not aware of any such legislation being enacted in Botswana.

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## Secured lending and credit (immoveables)

- 6 What principal types of security are taken on immoveable (real) property?**

The principal type of security for immoveable property is mortgage bonds.

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## Secured lending and credit (moveables)

- 7 What principal types of security are taken on moveable (personal) property?**

The principal types are general bonds, pledges, deeds of hypothecation and notarial bonds.

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## Unsecured credit

- 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

Pre-judgment attachments are ordinarily not available except in instances of enforcement of a landlord's hypothec (ie, common law mortgage) and attachments to found jurisdiction. Otherwise, a creditor must ordinarily commence action and obtain judgment before such creditor can become entitled to attach the debtor's assets in execution of the judgment. No special procedures apply to foreign creditors except that when a non-resident creditor commences action against a resident defendant, such defendant can demand security for costs in respect of the intended litigation. Previously there was a backlog of cases pending at the High Court, and in defended actions referred to trial, there was a waiting period of two to three years for the allocation of trial dates. This has changed since the introduction of judicial case management in May 2008. Trial dates can in practice be obtained within six months of the commencement of the action.

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## Voluntary liquidations

- 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?**

Where a company is unable to pay its debts as and when they fall due for payment in the ordinary course of business, the company is technically insolvent and must apply for voluntary liquidation. The company can by resolution present a petition to the High Court for its winding-up if its liabilities exceed its assets and it has no prospects of improving its financial situation and is therefore trading in insolvent circumstances. A debtor (natural person) may commence voluntary sequestration by filing a petition at the High Court surrendering his or her estate.

The commencement of liquidation proceedings has the effect of automatically depriving the petitioner or debtor of contractual capacity. This role is assumed by the trustee or liquidator, as the case may be, who will then, under the supervision of the master of the High Court, have control over all the affairs of the petitioner or debtor. All legal proceedings and execution of judgments against the assets of the petitioner or debtor are suspended unless otherwise authorised by the court.

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## Involuntary liquidations

- 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

A creditor who is owed a minimum statutory amount may make statutory demand for payment. Failure to pay constitutes an act of insolvency by the debtor, which will entitle the creditor to present a petition for liquidation or sequestration of the debtor. If a creditor is also able to demonstrate that the debtor's liabilities by far exceed its assets, thereby making the debtor factually insolvent, the creditor can apply for liquidation. The effects are similar to those stated in question 9.

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### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Reorganisation in Botswana falls under judicial management. This involves the appointment of a judicial manager to take over the managerial functions of the directors of the company. This process is adopted where even though a debtor is unable to pay its debts as and when such debts fall due for payment in the ordinary course of business and yet the debtor has ample assets and pending commercial transactions that would translate into cash at a later stage for the benefit of creditors, and therefore makes the debtor's business viable in the long term. In such a situation, the court will at the instigation of the directors of the debtor company or a creditor appoint a judicial manager to manage the financial and business affairs of the debtor for the benefit of all creditors. The judicial management order is usually discharged once the debtor's cash-flow situation improves or a majority of the creditors have been paid, or both, or once the debtor is able to settle debts incurred in the ordinary course of business as and when they fall due for payment.

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### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

In instances where a creditor can demonstrate that a debtor has a sound business but has cash-flow or management problems (usually due to mismanagement by directors of the debtor), or both, such a creditor can apply for the judicial management of the debtor's business by an independent third party (judicial manager). Commencement of the judicial management process means the mandate and functions of the directors of the debtor company are taken over by the judicial manager, who will be mandated by the court to manage the debtor's affairs for the benefit of the general body of creditors until such time that the court so directs.

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Where the directors of a company realise that the company is unable to pay its debts as and when they fall due for payment in the ordinary course of business, they must file a petition for liquidation. The directors have a legal obligation not to incur a liability that they know the company will not be able to satisfy when the obligation for payment becomes due. Should the directors continue trading in those circumstances, they would be causing the company to knowingly trade in insolvent circumstances, which would render the directors personally liable for any such debts thereby incurred by the company. The directors are therefore under an obligation to commence insolvency proceedings as soon as they determine that the company will not be able to pay its debts as and when they fall due for payment in the ordinary course of business. Shareholders are also liable and are required to contribute up to the maximum of any shares not yet paid up. Shareholders who ceased being shareholders one year before the petition for winding up is presented are not liable.

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

The court issuing the judicial management order can impose conditions that it deems fit or believes would assist in resolving the problem or ensuring that the creditors are paid and the company rescued.

Any costs incurred after the judicial management order is issued are deemed to be costs of administration and are paid prior to any

dividends to the pre-judicial management creditors. Accordingly creditors who supply goods and services to the judicial manager will be paid first as such costs would have been incurred in the judicial management of the debtor.

Before judicial management, creditors' views are solicited in creditors' meetings after presentation of regular reports by the judicial manager to the general body of creditors. The creditors usually give directions to the judicial manager at such creditors' meetings convened for that purpose.

A judicial management order is usually a provisional order and the judicial manager is obliged to submit regular reports to the court through the master of the High Court (the master). If the judicial manager at any point forms the view that the judicial management order is not serving its purpose and the debtor's financial situation is unlikely to improve, he or she may apply for liquidation or winding up of the company. Directors cease to act the moment a petition for winding up is presented to the court. A provisional liquidator appointed by the court exercises the function of the directors until a liquidator is appointed.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

In both judicial management and liquidations all legal proceedings (including the levying of execution) against the debtor are suspended and cannot be proceeded with except with the permission of the court. Legal proceedings can, however, be pursued against both the liquidator and judicial manager in the event of disagreement on issues affecting any interested party, including creditors of the estate.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

The liquidator or judicial manager may obtain loans to perform his or her mandate. Such loans are considered as administrative costs and rank above all claims and as such are settled first, before the settlement of all other claims.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Creditors are entitled in specified circumstances and in consultation with the master and liquidator (as set out in the Insolvency Act) to set off their claims.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

When a company is under judicial management, the judicial manager's mandate is usually to rehabilitate the company and not to sell its core assets, that is, assets used in the ordinary course of business to generate income. In that regard the judicial manager is entitled to continue the debtor's normal business until the debtor company is fully rehabilitated. However, in liquidations, the mandate is different. The mandate in that instance is to sell the assets of the liquidated company either as a going concern or piecemeal, whichever would, in the opinion of the liquidator, be to the benefit of the general body of creditors. The above notwithstanding, the liquidator is not entitled to sell any of the assets prior to the first creditors' meeting unless authorised to do so by the court. Our law does not allow for 'stalking horses'. Once a sale

agreement is concluded and finalised, no further bids can be accepted. A creditor cannot purchase assets in the estate by reducing its claim in the estate. A creditor may purchase assets and pay for same and also prove its claim in the estate and wait for the publication of the final liquidation and distribution account as well as the actual distribution of the proceeds or dividends in due course.

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### Intellectual property assets in insolvencies

- 19** May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

An IP licensor does not automatically acquire the right to terminate the debtor's right to use a particular licence unless the underlying contract makes provision for such termination (due to breach of contractual obligations) under those circumstances. Executory or incomplete contracts can be enforced by the liquidator against any entity that is a party to that contract. The liquidator is entitled to choose either to continue with the original underlying terms for use of the licence, to negotiate new terms or to terminate the contract altogether. The liquidator's decision will usually be based on the best interests of the estate and general body of creditors. Any creditor having an interest or aggrieved by the liquidator's decision, including the IP licensor, can apply to court to set aside the liquidator's decision if aggrieved by it.

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### Personal data in insolvencies

- 20** Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

See [www.gettingthedealthrough.com](http://www.gettingthedealthrough.com).

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### Rejection and disclaimer of contracts in reorganisations

- 21** Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

No such procedure exists in Botswana unless it can be shown that the contract seeks to unfairly prefer one concurrent creditor over the others. A provisional liquidator or, once confirmed, a liquidator has the option and may decide to cancel a lease agreement within three months of the sequestration.

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### Arbitration processes in insolvency cases

- 22** How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Insolvency proceedings in Botswana are statutory and fall within the jurisdiction of the High Court. Only the court has power to declare an entity insolvent. The court may, on application, consider and refer other disputes to arbitration but not the issue relating to determination of the solvency of the debtor.

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### Successful reorganisations

- 23** What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

There are no mandatory statutory requirements for a reorganisation plan. A company placed under judicial management can at any time

apply for the discharge of the judicial management order if the conditions that triggered the initiation of judicial management proceeding improve and creditors' claims have been satisfied, or if the debtor's cash flow or financial affairs have improved, thereby making it unnecessary for the judicial management order to continue. Court approval of the discharge of the judicial management order is mandatory. Non-debtor parties can only be released where creditors' claims have been satisfied.

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### Expedited reorganisations

- 24** Do procedures exist for expedited reorganisations?

There are no procedures for expedited reorganisations in Botswana.

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### Unsuccessful reorganisations

- 25** How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

An application for judicial management can be opposed on the grounds that the intended reorganisation was unlikely to yield the desired or proposed result. If the judicial management order is made and any terms imposed by the court are not met, the court may discharge the judicial management order and liquidate the debtor company.

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### Insolvency processes

- 26** During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

Once the provisional liquidator has been appointed, he or she is obliged to notify all known creditors and advise them of the current status of the liquidation and the collection of claim forms to be submitted and proved at the first creditors' meeting. It is not common practice to form committees and there are no statutory provisions for such committees. Notices of all creditors' meetings are published in the government gazette. The liquidator has an obligation to report to the master of the High Court.

The liquidator, at the direction of the creditors, may pursue claims against third parties. Creditors may only pursue claims against third parties with the express permission of the liquidator if the claim belongs to the estate, otherwise the liquidator may be cited as having an interest in the outcome of that litigation.

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### Enforcement of estate's rights

- 27** If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

The liquidator is entitled to request contributions from creditors to pursue claims in the interests of the general body of creditors. Additionally, the liquidator can also obtain loans to administer the estate until enough cash becomes available to the estate. Any such loan is considered a cost of administration and therefore paid prior to the payment of dividends to creditors.

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### Creditor representation

- 28** What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Creditors can, at their own expense, appoint legal representatives to act for them and represent them at creditors' meetings.

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**Insolvency of corporate groups**

- 29** In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Proceedings cannot be combined. Companies are considered to be separate entities and exist independently of each other irrespective of whether or not they are subsidiaries. It may be that the effect of liquidating a parent company will be that the subsidiary companies may be sold off by the liquidator and thereby exist independently of the liquidated estate of the principal debtor. There are no legislative provisions allowing the transfer of assets from an administration in Botswana to an administration in another jurisdiction.

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**Appeals**

- 30** What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

See [www.gettingthedealthrough.com](http://www.gettingthedealthrough.com).

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**Claims**

- 31** How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Creditors' claims are submitted and pursued through the liquidator, who as soon as practicable after his appointment as provisional liquidator must circulate claim forms to all known creditors. The completed claim forms must reach the master's office via the liquidator at least 24 hours before a scheduled and advertised creditors' meeting.

All creditors' claims are proved in creditors' meetings the validity of all creditors' claims is tested. Any creditor may with good reasons oppose the acceptance of a particular creditor's claim. A creditor whose claim is not accepted can apply to the High Court for determination of the validity of the reasons for disallowing the claim.

Transfer or purchase of claims against the debtor can be done by way of cession of the rights pertaining to the claims. A claim acquired at a discount can be enforced for its full value provided what is ceded is the full value. Interest accrues only up to the date of sequestration and not after.

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**Modifying creditors' rights**

- 32** May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The ranking of creditors' claims is prescribed by statute. The court's role in the process is to determine disputes, enforce statutory provisions and enforce agreements. The court cannot modify what has been prescribed by statute. Such modification is therefore rare, if it happens at all.

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**Priority claims**

- 33** Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

The only claims that rank above the secured creditors are costs incurred in the administration of the liquidated estate. Taxes due to the government are ranked as preferred claims and these are only paid after the secured creditors have been paid.

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**Employment-related liabilities in restructurings**

- 34** What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Employee claims are preferred claims and rank just below secured creditors. The liquidator, in the event that he decides not to continue the business of the insolvent, can give notice to the employees terminating the employment contract.

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**Pension claims**

- 35** What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Employees' claims against the insolvent rank as a preferred claim immediately below secured creditors and such claims are protected as such by the Employment Act.

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**Environmental problems and liabilities**

- 36** In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The insolvency administrator, in the case of Botswana the liquidator, replaces the insolvent in all transactions and bears the same liability as the insolvent in respect of all transactions inclusive of environmental issues. Accordingly, the liquidator remains responsible for addressing any environmental issues that may arise.

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**Liabilities that survive insolvency proceedings**

- 37** Do any liabilities of a debtor survive an insolvency or a reorganisation?

There are no statutory provisions prescribing that any liability is carried over after distribution of the assets of the estate.

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**Distributions**

- 38** How and when are distributions made to creditors in liquidations and reorganisations?

Payments of dividends to creditors are made after presentation of the final distribution and liquidation accounts to the master by the liquidator.

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**Transactions that may be annulled**

- 39** What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

Any creditor that disagrees with the amount of payment or ranking of any proposed distribution is at liberty to apply to the High Court stating the reasons why a particular payment should not be made. If the transaction is reversed, and unless the court orders otherwise, the proceeds thereof revert to the liquidator for distribution among the general body of creditors in accordance with the creditors' rankings.

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**Proceedings to annul transactions**

- 40** Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The criterion for voidable transactions is prescribed in terms of the Insolvency Act. Payments made to a particular creditor preferring it over other creditors can be challenged if made six months before the liquidation of the debtor.

**Directors and officers**

- 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

No, unless it can be demonstrated that the directors of the debtor traded recklessly or in insolvent circumstances.

Directors of the debtor become personally liable if it is demonstrated that they caused the debtor to trade in insolvent circumstances.

**Groups of companies**

- 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

We are not aware of any legislative provision that vests the court with power to order distribution in any other format outside what is provided in the Insolvency Act.

Usually the entity that is liquidated is the entity that will be the focus of the liquidator and the creditors. In the event holding companies are shareholders in the liquidated entity then their liability would be as defined by the applicable legislation.

**Insider claims**

- 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

A liquidator is empowered to investigate claims and call back any payment previously made that is deemed to be void or voidable by him or her within six months of such payment being made.

**Creditors' enforcement**

- 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

No such proceedings exist to allow creditors to seize assets of the debtor without court involvement. The court, through the master, regulates the activities of the liquidator and the estate until dividends are distributed to the creditors.

**Corporate procedures**

- 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

The Insolvency Act as read with the Companies Act regulates the process for liquidation of corporate entities. The Insolvency Act regulates the affairs of a natural person whose estate is sequestrated.

**Conclusion of case**

- 46 How are liquidation and reorganisation cases formally concluded?**

Cases are concluded by the filing of a final liquidation and distribution account at the office of the master and the subsequent distribution of dividends in accordance with such published accounts.

**International cases**

- 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Botswana has legislation on the recognition of foreign judgments and the minister is empowered to publish a list of countries whose judgments will be recognised in Botswana.

Botswana is not a signatory to the UNCITRAL Model Law.

**COMI**

- 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

This is not applicable in Botswana.

**Cross-border cooperation**

- 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

There are no legislative provisions covering this scenario.

**Cross-border insolvency protocols and joint court hearings**

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

This is not applicable in Botswana.

\* The content of this chapter is accurate as of November 2015.

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# Brazil

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

In Brazil, the main applicable law to corporate insolvencies and reorganisations is Federal Law No. 11,101/2005, known as the Brazilian Bankruptcy and Restructuring Law (BRL), which was enacted on 9 February 2005 and came into effect on 9 June 2005, bringing significant changes to the legal treatment of Brazilian companies that are insolvent or facing financial difficulties.

There is no specific condition that defines a company as 'insolvent' and the analysis of a 'insolvency state' that justify the insolvencies and reorganisations is more related to an economic crisis the company may be facing and to its inability to pay its creditors in a timely manner. However, generally, a company is considered insolvent if its debts exceed its assets.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

According to the BRL, the competent court to ratify out-of-court reorganisation plans, grant judicial reorganisation proceedings or declare the forced liquidation of a company is the estate court of where the main establishment of the company is located. Some judicial districts have courts that specialise in insolvency proceedings, but if not, the proceedings will be conducted by regular civil courts. In judicial reorganisation proceedings, the court in charge has jurisdiction over all matters concerning the disposal or encumbrance of the debtor company's assets, but all other matters should be processed according to their respective jurisdictions. In the case of forced liquidation proceedings, the bankruptcy court has jurisdiction over all matters concerning the debtor company.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Under the common denomination of 'debtors', the BRL specifies that both 'individual businessmen' and 'business companies' are subject to its provisions. The BRL also specifies that it shall not apply to state-owned companies and mixed-capital companies. Also exempted from the BRL are financial institutions, credit unions, social security entities, health-plan operators, insurance companies and other similar entities.

In a judicial reorganisation, only assets that are not part of the company's permanent assets may be sold regardless of creditors or judicial authorisation. In forced liquidation proceedings, all assets must be collected and sold by the judicial administrator, except those that are no longer property of the debtor because of fiduciary transfer of assets.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The Brazilian Federal Constitution provides that state-owned companies and mixed-capital companies shall receive the same legal treatment accorded to private companies, including commercial, labour and tax rights and obligations. Therefore, many scholars and practitioners understand that general insolvency laws such as the BRL should also apply to state-owned companies and mixed-capital companies, especially if they developed economic activities and not only provided public services.

Regarding financial institutions, such as credit unions, social security entities, health-plan operators, insurance companies and other similar entities, the exception in these situations is less controversial. Given the particular characteristics of such entities, lawmakers decided that their insolvency regimes should be defined in specific statutes. In any event, the provisions of the BRL shall also apply on a subsidiary basis to complement the statutes currently governing the insolvency regime of these entities.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Brazil has no specific legislation to deal with financial difficulties of institutions considered 'too big to fail'.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

The two main types of security taken on immovable (real) property are mortgage and fiduciary transfer of assets. In the case of a mortgage, the debtor maintains the property of the asset and will only lose it if the credit is enforced and the asset is sold in a judicial auction or adjudicated by the creditor. In the case of fiduciary transfer, the property is transferred to the creditor, and it has the right of repossession of the property in the event of default. Both securities must be fully registered and give the creditor special treatment in the case of judicial reorganisation or forced liquidation proceedings.

In a judicial reorganisation proceeding, creditors secured by mortgage or pledge are a specific class of creditors and will be paid according to the provisions of the approved and ratified reorganisation plan; and in a forced liquidation proceeding, these creditors are the second in the ranking of creditors for payment purposes, which is applied after the payment of priority creditors. Credits secured by fiduciary transfer of assets are not subject to judicial reorganisation or forced liquidation proceedings, meaning that they may enforce the respective contracts and securities even if the debtor company is facing an insolvency proceeding.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

The two main types of security taken on moveable (personal) property is pledge and fiduciary transfer of assets. In the case of a pledge, the debtor maintains the property of the asset and will only lose it if the credit is enforced and the asset is sold in a judicial auction or adjudicated by the creditor. In the case of fiduciary transfer, the property is transferred to the creditor and it has the right of repossession of the property in the event of default. These securities also give the creditor special treatment in the case of judicial reorganisation or forced liquidation proceedings.

In a judicial reorganisation proceeding, creditors secured by mortgage or pledge are a specific class of creditors and will be paid according to the provisions of the approved and ratified reorganisation plan; and in a forced liquidation proceeding these creditors are the second in the ranking of creditors for payment purposes, which is applied after the payment of priority creditors. Credits secured by fiduciary transfer of assets are not subject to judicial reorganisation or forced liquidation proceedings, meaning that they may enforce the respective contracts and securities even if the debtor company is facing an insolvency proceeding.

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## Unsecured credit

### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

In a judicial reorganisation proceeding, unsecured creditors are a specific class of creditors, and are paid according to the provisions of the approved and ratified reorganisation plan. In a forced liquidation proceeding, unsecured creditors are the sixth in the ranking of creditors for payment purposes, which is applied after the payment of priority creditors.

If there is no insolvency proceeding, unsecured creditors may collect or enforce their credits with different proceedings according to each type of debt instrument. Certain instruments allow the creditor to file an enforcement proceeding, which is less time-consuming and provides for the possibility of pre-judgment attachment of assets. Regular collection lawsuits are more-time consuming and do not allow pre-judgment attachment of assets. There is the possibility, however, of obtaining temporary restraining orders, if requirements are fulfilled.

There are no special procedures that apply to foreign creditors, only specific formal requirements for the filing of the lawsuits.

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## Voluntary liquidations

### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

According to the BRL, debtors that are facing an economic and financial crisis and do not meet the requirements to request their judicial reorganisation must request the declaration of their own forced liquidation. The debtor company must present the reasons why it believes that continuation of its business activities is not possible and present the following documents:

- accounting statements for the last three financial years and those drawn up especially to support the forced liquidation request, prepared in strict accordance with applicable corporation law and consisting necessarily of:
  - balance sheet;
  - accrued income statement;
  - profit and loss statement as from the last financial year; and
  - cash flow statement;
- a list of creditors, stating their addresses and the amount, kind and rating of the respective claims;
- a list of properties and rights constituting the assets, with an estimate of the respective value and title documents;
- evidence of his or her status as businessperson, articles of association or by-laws in effect, or if there are none a list of all partners, their addresses and their personal assets;
- the mandatory books and accounting documents required by law;

- a list of senior managers during the last five years, with their respective addresses, offices and equity holdings.

If the request is accepted by the bankruptcy court, the forced liquidation will be decreed. In this case, the debtor is removed from its activities and the existing assets are collected and sold by the judicial administrator named by the court. Any proceeds derived from the sale of assets are distributed among the creditors according to a preference order established by law. The claims demanding liquid amounts against the debtor company are suspended and transferred to the bankruptcy court.

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## Involuntary liquidations

### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Any creditor may request the forced liquidation of a debtor in certain circumstances, including the following:

- failure by the debtor to comply with payment obligations in excess of 40 times the prevailing Brazilian minimum wage, provided that a protest with a public registry has been lodged with respect to the corresponding indebtedness. To reach the above threshold, two or more creditors can combine their credits;
- existence of debt collection proceedings against the debtor where no assets have been attached or no money has been deposited to secure payment of the relevant obligations;
- the debtor has been engaged in actions such as unjustified sales of assets or fraudulent schemes against the interests of creditors; and
- failure by the debtor to comply with obligations under a judicial reorganisation plan.

The debtor company will be notified about the request, and will be able to pay the owed amount, request judicial reorganisation or present a defence. If the defence is not accepted and the other possibilities are not accomplished by the debtor company, its forced liquidation will be decreed, and the same effects mentioned in question 9 will take place.

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## Voluntary reorganisations

### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The debtor that meets certain conditions specified in the BRL may apply for a judicial reorganisation proceeding. The debtor must be facing an economic and financial crisis and must prove the following requirements:

- it shall not be bankrupt, and if it has been, the resulting liabilities shall have been discharged by final and conclusive decision;
- it shall not have engaged in judicial reorganisation within the last five years;
- it shall not have engaged in judicial reorganisation, within the last eight years, based on the special plan provided in the BRL for small business debtor companies; and
- it shall not have been convicted or does not have, as a senior manager or controlling partner, a person convicted of any of the crimes provided for herein.

Also, the request must be accompanied by several documents, such as:

- a statement of the causes of the debtor's equity condition and the reasons for the economic and financial crisis;
- accounting statements for the last three financial years and those drawn up especially to support the petition, prepared in strict compliance with applicable corporation law and consisting necessarily of:
  - the balance sheet;
  - accrued income statement;
  - income statement as from the last financial year; and
  - management report on cash flow and projection thereof;
- a full itemised list of creditors, including those under an obligation to do or to give, stating the address, type, rating and updated amount of the respective claim, and specifying its origin and schedule of payments as well as showing the accounting records on each pending transaction;
- a full list of employees, stating the respective functions, salaries, indemnities and other amounts to which they are entitled, with

- the corresponding accrual months, and specifying amounts pending payment;
- certificate of debtor's good standing at the Public Registry of Companies, coupled with updated articles of incorporation and minutes of appointment of current senior managers;
- a list of private assets of the debtor's controlling partners and senior managers;
- updated statements of debtor's bank accounts and of any financial investments of any kind, including those in investment funds or on stock exchanges, issued by the respective financial institutions;
- certificates of the protest offices in the judicial district of the debtor's domicile or headquarters and branches; and
- a list, signed by the debtor, of all lawsuits in which he or she figures as a party, including labour-related suits, with an estimate of the respective disputed amounts.

If the application is in proper form, the court will authorise the initiation of judicial restructuring proceeding. A public notice will then be included in the official gazette containing, among others: a summary of the request made by the debtor; a list of creditors; and a warning about the applicable term for any challenges to the list of creditors, including requests for adjustments and inclusions.

A judicial administrator will be nominated by the court to manage the proceeding; there is a 180 day stay period for claims subject to the proceeding (the ones existing at the date of the filing, whether matured or not, with few exceptions provided by law); and in principle, there will be no change in management. In certain circumstances, however, managers shall be removed from their positions, including when: there are indicia of bankruptcy crimes; they have acted with wilful misconduct or engaged in fraudulent schemes against creditors; they have been making personal expenditures that are not compatible with their income; or their removal is specified in the reorganisation plan.

The debtor company shall submit a reorganisation plan within 60 days of the publication of the court order authorising the initiation of the proceeding, to be analysed and accepted or not by the creditors.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

In Brazil, only the debtor company may request the commencement of its judicial reorganisation proceeding; there is no possibility of creditors doing so.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

According to the BRL, a debtor that is facing an economic and financial crisis and does not meet the requirements to request its judicial reorganisation must request the declaration of its own forced liquidation. However, the BRL does not provide for any penalty or liabilities for the debtor company that does not file for its own forced liquidation. There are also no specific consequences if a company carries on business while insolvent.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

The debtor company can carry on its business activities during reorganisation. The sale of permanent assets may only occur:

- if provided in the approved and ratified reorganisation plan; or

- if authorised by the bankruptcy court after the debtor company has proven the need of such sale and the creditor's committee (if there is any) has also agreed.

The creditors who supply goods or services to the debtor company after the filing for reorganisation will not be subject to the proceedings and the credits originated after the filing may be enforced, and in case of forced liquidation, will have priority of payment. The creditors, if not in a creditor's committee, have no active role in supervising the debtor's business activities.

In the course of judicial reorganisation proceeding, in principle there will be no change in management. Therefore, directors and officers will retain their positions, although working under the supervision of the creditors' committee (if any) and the judicial administrator.

In certain circumstances, however, managers shall be removed from their positions, including when:

- there are indicia of bankruptcy crimes;
- they have acted with wilful misconduct or engaged in fraudulent schemes against creditors;
- they have been making personal expenditures that are not compatible with their income; or
- their removal is specified in the reorganisation plan.

When regulating the removal of managers, the BRL initially states that they shall be replaced as provided for in the corporate documents of the debtor or in the reorganisation plan. But immediately following this provision, it provides another solution to the same scenario by specifying that the general meeting of creditors shall appoint a judicial manager.

In forced liquidation proceeding, the management of the company is substituted by the judicial administrator.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

In judicial reorganisation proceedings, a suspension of 180 days shall apply to all legal proceedings in course against the debtor, in relation to debts that are subjected to the proceeding. Upon the expiration of such term, all creditors regain the right to initiate or proceed with their lawsuits against the debtor. In practice, this term tends to be extended by bankruptcy courts. In forced liquidation proceedings, there is also the provision of suspension of all legal proceedings in due course against the debtor indefinitely, once all creditors must be paid within the proceeding, in accordance to a legal preference order.

There are two exceptions to the suspension rule: lawsuits where there are no pre-defined amounts being claimed, and labour claims, which shall continue their course in labour courts until the applicable labour credits are defined. In these two cases, the competent court may send an order to the court in charge of the restructuring proceedings establishing an estimated amount to be reserved in the names of the relevant creditors. Once such amounts are finally determined, they shall be included as credits in the restructuring proceedings.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

The company under reorganisation may continue its ordinary activities unless otherwise ordered by the court, which includes obtaining unsecured financing, so the debtor company does not need to obtain any approval towards the court to receive loans. Secured financing need to be judicially authorised if the security is a permanent assets. The BRL does not establish any special rights or preferences derived from financing obtained during the course of a judicial reorganisation; in the case of forced liquidation, it will be equal to other debts acquired by the debtor company during the reorganisation, although the reorganisation plan may provide some preference in order to attract potential investors. The type of security granted is very important to determine the rank of the credit related to the new loans.

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**Set-off and netting**

- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

The credits that are submitted to the reorganisation proceeding cannot, in principle, be offset with credits of the debtor company, once that according to the Brazilian Civil Code, the offset is a way of extinction (payment) of debts, and according to the BRL, no creditor can be paid to the detriment of other creditors that are also submitted to the proceeding, what can even be considered a bankruptcy crime. On the other hand, in a reorganisation proceeding, credits that are not submitted to the proceeding may be, as a rule, offset.

In a forced liquidation proceeding, the offset is possible. The debts that can be offset are the ones owed by the debtor company until the date of the judicial decree of the forced liquidation, and the Brazilian Civil Code must be followed for carrying out such offset. However, the offset is not possible with debts existing after the decree of the forced liquidation (with the exception of cases of merger, incorporation, split or death), and with credits that were transferred when the insolvency situation was already known or related to fraud or intention to harm. Generally, under a forced liquidation proceeding, the offset of debts does not require court approval.

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**Sale of assets**

- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

The reorganisation plan may provide for a judicial sale of branches or individual going-concerns belonging to the debtor. This also occurs in forced liquidation proceedings. The judicial sale may take the form of an auction, be effected through proposals submitted in sealed envelopes or be a combination of the former two options.

Once the judicial sale is effected, the relevant branch or going concern will, in principle, be free and clear of any liens and encumbrances, and the purchaser will not succeed the debtor with respect to any indebtedness. As a consequence, creditors will not be able to claim any amount from the purchasers of branches or going concerns, and the corresponding assets will not be attached to satisfy their credits. Therefore, creditors will simply retain their original claims against the debtor.

The BRL does not provide a 'stalking horse' bid, but these mechanisms have been recently used in sale proceedings, especially if provided in a judicial reorganisation plan and approved by the creditors.

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**Intellectual property assets in insolvencies**

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

In the case of judicial reorganisation proceeding, the IP licensor or the debtor company may only terminate the debtor's right to use it if the contractual provisions allow it to, and the contractual provisions and remedies must be observed. Also, the provisions of termination caused solely by the filing of the judicial reorganisation are considered null by Brazilian courts. In a forced liquidation proceeding, the judicial administrator may opt to maintain the agreement if it reduces or avoids the increase of the debts or if it helps to maintain and preserve the debtor company's assets, but it will not be able to terminate the agreement and continue to use the IP for the benefit of the estate.

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**Personal data in insolvencies**

- 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

There is no restriction in the BRL about the use of personal information or customer data collected in an insolvency proceeding or the transfer of the information, as an asset, to a purchaser.

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**Rejection and disclaimer of contracts in reorganisations**

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

The debtor company under reorganisation continues its business activities and directors and officers are not removed from its positions, as a rule. Also, the BRL has no provision on termination of contracts in the case of judicial reorganisation. Therefore, the debtor can reject or disclaim an unfavourable contract, but it must follow the contractual rules regarding the reasons of the rejection and the proceeding for it. If the debtor breaches the contract after the reorganisation is opened, the other party may use the contractual remedies, such as filing a claim and obtaining a credit right, if applicable, and this credit will not be subject to the reorganisation and may be enforced against the debtor company.

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**Arbitration processes in insolvency cases**

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Arbitration is not used specifically in insolvency proceedings, but is often used in commercial disputes and claims between parties. The arbitration claims involving the debtor company generally are not suspended in the case of judicial reorganisation, since in arbitration commonly there are no predefined amounts being claimed (exception for the stay period).

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**Successful reorganisations**

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

The debtor company shall submit a reorganisation plan within 60 days of the publication of the court order authorising the initiation of the proceeding. If the plan is not submitted, the debtor shall be declared bankrupt (as forced liquidation). The reorganisation plan must contain: a detailed description of restructuring mechanisms to be used, which may include debt rescheduling, corporate reorganisation, transfer of corporate control, partial sale of assets, leasing of going-concerns and a series of other measures; demonstration of the economic feasibility of the debtor's business; and a report on the debtor's assets prepared by an expert appraiser or company. The plan cannot provide that overdue labour credits and credits deriving from accidents at work will be paid in a term longer than one year from the ratification of the approved plan by the bankruptcy court.

Creditors will be informed about the reorganisation plan and the applicable term to challenge the plan through a public notice. If any objection to the proposed plan is submitted by any creditor, the court shall call a general meeting of creditors. In the meeting, creditors may approve the plan as originally proposed, approve a modified version of the plan, as long as there is no opposition from the debtor and no harm to absent creditors, or reject the plan, in which case the debtor should be declared bankrupt (as forced liquidation).

Any reorganisation plan must be approved by the following four categories of creditors in a general meeting of creditors:

- (i) labour creditors and creditors from accidents at work;
- (ii) secured creditors;
- (iii) unsecured creditors, creditors with special or general preference and subordinated creditors; and
- (iv) small business creditors.

In the first and fourth classes of creditors, approval is achieved with the favourable vote of the majority of creditors present at the meeting, regardless of the amount of their credits. In the other two classes, approval is achieved with the favourable vote of both creditors representing more than half of the credit amounts represented at the meeting and the majority of creditors present at the meeting.

If certain vote combinations specified in the BRL are recorded in the general meeting of creditors, the court may grant the judicial restructuring, even when the plan was not approved pursuant to the quorum requirements explained above, if some requirements are fulfilled (cram down).

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

Any debtor that meets certain conditions specified in the BRL may propose and negotiate with its creditors an expedited reorganisation plan, also called out-of-court reorganisation plan, and request its judicial ratification, with the possibility of enforceability towards of each category affected by the plan that did not adhere to it, if a certain quorum of adherence is obtained.

In other words, despite being deemed 'out-of-court', the plan must be ratified by a bankruptcy court to bind creditors who did not even adhere to the plan. This does not mean that the plan will be conducted within the context of court proceedings. It just needs to be judicially ratified.

To produce effects with respect to all creditors affected by the plan, including those that have not expressly adhered to the settlement, the BRL provides that the ratified plan must have been approved by creditors representing more than three-fifths of credits in each type of creditors contemplated by the plan.

Once the debtor requests the ratification of the plan, the creditors will have the opportunity to challenge such ratification. Nevertheless, any challenges may be based solely on an alleged illegality or a failure by the debtor to comply with all necessary legal requisites or formalities.

If the challenges are not accepted by the court, the out-of-court reorganisation plan will be ratified and be applicable to all creditors affected in the plan. The plan's provisions and obligations are judicially enforceable after the ratification decision.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

See question 23. If the debtor company fails to present a reorganisation plan in due time, its forced liquidation must be decreed. If the reorganisation plan is presented, creditors will be informed about the reorganisation plan and the applicable term to challenge the plan through a public notice. If any objection to the proposed plan is submitted by any creditor, the court shall call a general meeting of creditors. In the meeting, creditors may approve the plan as originally proposed, approve a modified version of the plan, as long as there is no opposition from the debtor and no harm to absent creditors, or reject the plan, in which case the debtor should be declared bankrupt (as forced liquidation).

If the debtor company fails to carry out the plan while the proceeding is still running, its forced liquidation should be decreed (but this usually does not happen, and the debtor company is given a chance to present a new plan); if the debtor company fails to perform the plan after the end of the reorganisation proceeding, the creditor may enforce the credit or request the forced liquidation in a independent proceeding.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The creditors are first given notice, through a public notice, about the decision that authorises the processing of the judicial reorganisation or the decision that decrees the forced liquidation, containing the list of creditors presented by the debtor company. After that, they are again given notice about the list of creditors presented by the judicial administrator. Then, the creditors will be notified about the presentation of the reorganisation plan, as applicable, and also about any general meetings of creditors that are scheduled. Any and all decisions of the proceedings are also published in the official gazette.

General meetings of creditors may be called upon request of bankruptcy court, the judicial administrator, creditor's committee or creditors holding at least 25 per cent of the claims in a determined class of creditors. General meetings of creditors are also called to discuss and vote on the reorganisation plan proposal and in other specific events provided in the BRL.

The judicial administrator has several duties and obligations, both in judicial reorganisations and forced liquidation proceedings, provided in section 22 of the BRL, including presenting monthly reports on the debtor company's activities, as well as providing any information requested by the bankruptcy court or the creditors.

As a rule, creditors may not pursue the estate's remedies against third parties, only if there are joint liability debtors or the corporate veil of the debtor company is disregarded.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

In a forced liquidation proceeding, creditor's may not pursue the estate's remedies, as the judicial administrator represents the bankrupt estate in order to pursue remedies against third parties. The fruits of the remedies belong to the bankrupt estate and will be used to pay the creditors according to the legal order of payment. In a judicial reorganisation proceeding, there is no bankruptcy estate and the debtor company continues to perform its activities.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The BRL contemplates an optional creditor's committee, and must be constituted of one creditor or the labour class, one creditor of the secure class, one creditor of unsecured class and one creditor of the micro businesses class. However, the creditor committee is rarely constituted in Brazil, since creditors can vote, negotiate and take part of the proceedings even if they are not in the creditors' committee. Additionally, members of the creditors' committee can be held liable for the outcome of the proceedings (even if they do not have the intention to harm third parties, creditors or the debtor company). The expenses of the committee may be paid by the debtor company.

The creditor's committee has the following duties, among others:

- to monitor the activities carried out by the debtor and the judicial administrator and present monthly reports about them;
- to inform the court in the event it detects any violation or harm of the creditors' rights;
- monitoring the fulfilment of the restructuring plan; and
- when managers are removed and until the restructuring plan is approved, request court authorisations for sales of assets, borrowings and the creation of security interests to ensure the continuation of business activities.

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### Insolvency of corporate groups

- 29** In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

The filing of an insolvency proceeding does not have a direct impact on a parent, subsidiary or an affiliate company of the debtor, considering that only companies that make the request are considered under reorganisation or forced liquidation. There are grounds for procedurally consolidating insolvency proceedings involving related parties – it is actually common for companies of the same economic group filing together for reorganisation, and commonly accepted by courts. However, there is case law discussion about substantively consolidating insolvency proceedings – whether the reorganisation plan should or could be the same, or not – and each court has its own understanding on the matter. There is no provision under the BRL addressing the transferring of assets between countries.

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### Appeals

- 30** What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

The right to appeal is usually derived from the BRL and Brazilian Code of Civil Procedure, if all the requirements are fulfilled; there is no need for permission to appeal. There is also no provision of any requirement to post a security in order to proceed with an appeal. The main appeals applicable to insolvency proceedings are: interlocutory appeal, appeal from final judgment and motion to stay foreclosure.

The following decisions are subject to interlocutory appeals: the decision that authorises the processing of the reorganisation proceeding, the decision about judicial proof of claims, the decision that ratifies the reorganisation plan, the decision that decrees the forced liquidation of a company and any other interlocutory decision. Appeals from final judgment must be presented against the decision that ends the reorganisation proceeding, the decision that denies the request of forced liquidation, the decision that ends the forced liquidation proceeding, the decision about the request for restitution (fiduciary sale of assets), the decision about requests for annulment of acts and the decision that ratifies the out-of-court reorganisation plan. Motions for clarification may be presented every time there is a material error in a decision or the decision is unclear, contradictory or silent about something that should be analysed.

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### Claims

- 31** How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

In both judicial reorganisation and forced liquidation proceedings, the creditors have the possibility of presenting a statement of credit to the judicial administrator against the first list of creditors presented by the debtor company and published through a public notice, to discuss the amount and classification of its credit. The term for presentation is 15 days. The judicial administrator will analyse the statement of credits and a new list of creditors will be published. Then, the creditors have the possibility of presenting a proof of claim to the bankruptcy court in 10 days, which will analyse such claims and decide on the definite amount and classification of the credits. If the creditors do not present the statement of credit in due term, it will be considered a late statement of credit and be processed as a proof of claim. The creditor may present an interlocutory appeal against the judicial decision of its proof of claim. The transfer of claims is possible and must follow the requirements of the Brazilian Civil Code, including the claim for contingent or unliquidated amounts, which will be determined in specific lawsuits.

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### Modifying creditors' rights

- 32** May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

In terms of a forced liquidation proceeding, the court may not change the rank of a creditor's claim, since such rank is determined by the BRL. In the case of a judicial reorganisation proceeding, there is no rank of claims, but classes of creditors that will be paid according to the provisions of the approved and ratified judicial reorganisation plan.

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### Priority claims

- 33** Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

In judicial reorganisation proceedings, there are no other privileged or priority claims, considering that all credits subject to the proceeding will be paid according to the provisions of the approved and judicially reorganisation plan.

In forced liquidation proceedings, credits secured by fiduciary transfer of assets and credits derived from business with the debtor company's after the request for judicial reorganisation may be considered privileged, considering they will be paid before the creditors in the rank of payment. In the rank of payment, only employee-related claims have priority over creditors secured by mortgage or pledge.

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### Employment-related liabilities in restructurings

- 34** What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

There is no specific provision in the BRL regarding termination of employment agreements. In the judicial restructuring proceeding, considering that the debtor company continues to practice its business activities, the employment agreements remain in force and may be terminated by the regular legal hypotheses (dismissal with just cause, dismissal without cause, employee's resignation and indirect dismissal). In the case of forced liquidation proceeding, with the sale of the debtor company's assets, all employment agreements of the encompassed employees will be automatically terminated and new agreements must be entered into with the purchaser, if the purchaser has such intention.

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### Pension claims

- 35** What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

In Brazil, entities that must pay pension-related claims, such as government and financial institutions, are not allowed to file reorganisations and may not be liquidate under BRL.

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### Environmental problems and liabilities

- 36** In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Environmental problems are not subject to reorganisation proceedings and must be dealt with directly by the debtor company, which is not exempt from its environmental obligations of controlling and remediating damaged caused. Environmental liabilities of shareholders, directors, officers and third parties will be determined by specific environmental laws, with no possibility of being imposed on creditors.

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### Liabilities that survive insolvency proceedings

- 37** Do any liabilities of a debtor survive an insolvency or a reorganisation?

In a judicial reorganisation proceeding, any credit that exists on the date of filing, even if it not matured, is covered by the proceeding and cannot be enforced by the creditor within the stay period. However, some specific types of credits are excluded from proceedings and may be

immediately enforced; this means that these liabilities remain intact. The credits are: tax credits, creditors with title to assets and foreign exchange advancements credits. Credits that are subject to the proceeding will be paid according to the reorganisation plan and are due until their payment. If not paid in due time while the proceeding is still running, they may cause the decree of forced liquidation; if not paid in due time after the end of the proceeding, the credit may be enforced.

In forced liquidation proceedings, only credits secured by fiduciary sale of assets are excluded from the proceeding – they must, however, file a request for restitution in the proceeding in order to repossess the assets given in guarantee and that does not belong to the debtor company any more. All the debtor company's obligations will be considered extinguished if it is able to pay all of its debts, if it is able to pay up to 50 per cent of its unsecured debts, after five years of the end of the proceeding, or after 10 years of the end of the proceeding if there was any conviction for a bankruptcy crime.

The reorganisation plan presented by a debtor company may provide for a judicial sale of branches or business units belonging to the debtor, which can also occur in a forced liquidation proceeding.

A judicial sale, according to section 1425 of the BRL, may:

- take the form of an auction;
- be effected through proposals submitted in sealed envelopes; or
- be a combination of these two options.

Once a judicial sale is effected, the relevant branch or business unit will be free and clear of any liens and encumbrances, and the purchaser will not succeed to the debtor with respect to any indebtedness. As a consequence, the creditors of the debtor company are not able to claim any amounts from the purchasers of branches or business units, and the corresponding assets cannot be enforced upon to satisfy the debt.

## Distributions

### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In reorganisation proceedings, creditors that are subject to those proceedings will be paid according to the approved and ratified reorganisation plan. In the forced liquidation proceeding, creditors will be paid with the proceeds of the sale of the debtor company's assets according to the legal order of payment, below:

- labour claims of up to 150 times the prevailing minimum wage for each creditor, and claims deriving from accidents at work;
- secured credits up to the value of the relevant collateral;
- tax debts;
- credits with special privileges;
- credits with general privileges;
- unsecured credits;
- contractual penalties, tax penalties and fines deriving from violations of legal provisions; and
- subordinated credits (as considered by law or agreement, and shareholders' and certain managers' credits).

Some credits should be prioritised and paid before all of those mentioned above, in the order set forth below:

- the compensation payable to the trustee and his or her assistants, and labour-related claims or occupational accident claims referring to services rendered after the decree of the forced liquidation;
- sums provided to the bankruptcy estate by the creditors;
- expenses with schedules, management, asset sale and distribution of the proceeds, as well as court costs of the forced liquidation proceedings;
- court costs with respect to actions and enforcement suits found against the bankruptcy estate; and
- obligations resulting from valid legal acts performed and contracts agreed during the judicial restructuring proceeding, such as loans and continuity of supply, or after the decree of the forced liquidation, and taxes relating to triggering events postdating the decree of the forced liquidation.

In addition, if the debtor is in possession of assets (including money) that belongs to third parties at the time the forced liquidation is decreed (by a leasing or fiduciary sale agreement or advance of foreign exchange currency agreement, for example), rightful owners may request restitution of their assets before the payment of any creditor, which may be

understood also as a priority over the order of preference of the BRL. This is the case because such assets (which may include money) are understood by law and case law to not belong to the debtor, and, therefore, cannot be included as part of the bankruptcy estate.

## Transactions that may be annulled

### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The BRL contains a list of actions that shall produce no effects with respect to the bankruptcy estate, regardless of whether the parties were aware of the financial difficulties facing the debtor or whether there was any fraudulent intent. Such actions are deemed incompatible with the reasoning underlying the BRL. Accordingly, they may be disregarded automatically by the court or at the request of any interested party.

Actions considered ineffective include, for instance:

- payment of unmatured debts during the suspect period;
- payment of overdue debts effected during the suspect period in a manner that is different from what was established in the original agreement;
- the creation of security interests during the suspect period to secure payment of pre-existing indebtedness; and
- donations and other equivalent actions effected within the period of two years preceding the forced liquidation.

In addition to those actions deemed automatically ineffective, any action aimed at intentionally defrauding creditors may be revoked. In this case, however, the party seeking the revocation must prove, in a separate lawsuit, that there was a fraudulent scheme arranged between the debtor and a third party, and that the bankruptcy estate actually suffered damages as a result of such scheme.

The bankruptcy legal term, also known as the 'suspect period' or 'look back period', shall be set by the court upon the declaration of forced liquidation. It may retroact until 90 days before:

- the forced liquidation request;
- the application for judicial restructuring later converted into forced liquidation; or
- the first protest for non-payment lodged against the debtor.

Regarding reorganisation proceedings, there are no specific provisions under the BRL Bankruptcy Law in order to nullify or void certain acts of the debtor. However, creditors may opt to file lawsuits to nullify or void these acts in accordance with the Brazilian Civil Code and Code of Civil Procedure.

## Proceedings to annul transactions

### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

See question 39. There is no suspect period if the debtor company is in reorganisation (acts may be annulled or considered void in spite individual claims), however, this period may be considered in case the forced liquidation is decreed. Creditors may also attack voidable transactions.

## Directors and officers

### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

In forced liquidation proceedings, shareholders, controlling shareholders, directors and executive officers may be considered liable for debts or acts, or both, if the court understands that some requirements were fulfilled.

Regarding this topic, the BRL provides that the bankruptcy court may investigate and determine shareholders, controlling shareholders, directors and executive officers liabilities if it verifies that they performed any act or omission that contravenes Brazilian law – such as corporate laws, tax laws and labour laws, among others – regardless of

### Update and trends

The current economic and political crisis in Brazil, the volatility in the global market and the rise in corporate restructurings have had no impact on Brazil's insolvency regime so far. However, these events have had significant impact on the analysis made by the courts when judging appeals related to insolvency proceedings, with stricter control over the companies.

The most important amendments currently envisaged are:

- Legislative Bill No. 314/2014, which intends to alter the name of the BRL to the 'Ramez Tebet Law'. It has already been approved by the Brazilian Senate and is currently in the Brazilian House of Representatives for analysis. Ramez Tebet was a former senator and participated significantly in the drafting of the BRL; and
- Legislative Bill No. 5,587/2013, from the Brazilian House of Representatives, already sent to the Senate under No. 191/2015, which adds a paragraph to the BRL regulating the extension of the bankruptcy effects to affiliated companies and companies controlled by the debtor, when there is strong influence of a corporate economic group in the other, and the intention of harming creditors.

the collection of the assets and impossibility of paying all the creditors of the company.

As an example, the Brazilian Corporate Law sets forth, in its section 116, the definition and the rules of conduct that shall be observed by the controlling shareholder, and section 117 provides the liability rule applicable to the controlling shareholder. Also, section 153 et seq provides the duties of the company's directors and executive officers, and in the case of violation of such duties or illegal acts in conducting social businesses, the managers shall be deemed liable for their acts.

So, in principle, if the company's shareholders or managers have contravened one of the sections mentioned above, there is a possibility that the court will make them responsible for certain obligations and acts, even if they are pre-bankruptcy actions.

The BRL also predicts that in those cases, a responsibility lawsuit will begin in the bankruptcy court, and in this lawsuit, the defendant's assets can be blocked in a compatible amount to the damage caused, until final judgment. The term for the filing of such lawsuit is two years after the decision that ends the forced liquidation proceeding becomes unappealable.

Apart from that, based on section 50 of Brazilian Civil Code, the court may disregard the company's corporate veil, if it considers that there was an abuse of its legal personality (in the case of equity confusion and misuse of purpose). In this case, the shareholders would be considered liable of all the company's debts.

Finally, the public prosecutor may understand that the shareholders, officers or directors committed a bankruptcy crime and file a criminal action, considering that section 179 of the BRL determines that the shareholders, executive officers, directors and counsellors will be equivalent to the debtor company for the criminal effects of the BRL. Also, the BRL sets out several criminal offences related to bankruptcy, the penalties for which can vary from one to six years' imprisonment plus fine.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

As already mentioned above, the filing of an insolvency proceeding does not have a direct impact on a parent, subsidiary or an affiliate company of the debtor, only once the company that makes the request is considered under reorganisation or forced liquidation. However, parent, subsidiary or affiliated companies may be held responsible for the debtor company's liabilities in case of recognition of economic group and piercing of the corporate veil. The essential requirements are: abuse of the corporate veil, with deviation of the company's purpose or assets confusion, or both, between the companies. In each concrete case, the judge will analyse the presence of such requirements – these requirements are more objective than just 'fraud' or 'abuse', but the decision by the court remains very subjective.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

In judicial reorganisation proceedings, insider claims of the debtor company's shareholders or parent, subsidiary or affiliate company will be ranked as unsecured and do not have voting rights in the general meeting of creditors. In forced liquidation proceedings, insider claims are classified as subordinated claims, which are the last in the legal order of payment.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Seizure of assets is not possible outside of court proceedings. In the case of fiduciary sale of assets, the creditor has the right of repossession of the property in the event of default, through administrative proceedings and after an auction, if no acceptable bids are presented.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Yes, the Brazilian corporate legislation provides for a winding-up proceeding. Technically, the winding up of a Brazilian company is the termination of the corporate entity itself. Therefore, normally the winding up encompasses three steps:

- dissolution triggering event;
- liquidation of all company's assets and liabilities; and
- termination of the legal entity and cancellation of board of trade entries and other enrolments with authorities.

According to Brazilian law, a company may be dissolved for several different reasons, such as:

- expiration of company's term, unless the company remains for a undefined term;
- quotholders' or shareholders' resolution, according to specific quorums;
- lack of business operational authorisation;
- judicial annulment of incorporation;
- exhaustion of corporate purpose, or the same is held impossible; and
- upon dissolution conditions if provided for in the articles of association.

Finally, the law also provides for the termination without dissolution or even liquidation, in the case of transformation, merger, consolidation or split. In such cases, the law provides for specific succession for the assets and liabilities of the terminated company, and on the protection of creditors' rights.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Judicial restructuring proceedings shall remain in place until all obligations maturing within two years that are specified in the plan are fully complied with by the debtor. If the debtor fails to comply with any obligation within such period, its forced liquidation it shall be declared. Any obligation unfulfilled after the two-year period entitles creditors to initiate collection proceedings or request the declaration of the debtors' forced liquidation.

Verifying that all obligations maturing within two years were fulfilled, the court shall order the termination of judicial restructuring proceeding. It should be noted that, although no longer subject to court proceedings, the debtor remains liable for all obligations specified in the plan that are still outstanding.

Regarding forced liquidation proceedings, after being judicially decreed, the debtor company will be liquidated so that its assets can be attached and sold by the judicial administrator, and the amount

obtained will pay the creditors. Only after the extinguishment of all obligations may the shareholders request the rehabilitation of the company, in order to explore its activity once again.

All the debtor company's obligations will be considered extinguished if it is able to pay all of its debts, if it is able to pay up to 50 per cent of its unsecured debts, after five years of the end of the proceeding, or after 10 years of the end of the proceeding if there was any conviction for a bankruptcy crime.

The forced liquidation proceeding is a case of total judicial dissolution of the company. If, after the selling of all assets and the payment of creditors, there is any amount left – which is hard to discern – this amount will be given to the shareholders in proportion to their participation in the company's equity.

#### International cases

**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

There is no specific recognition or relief provision in Brazil concerning an insolvency proceeding in another country. Also, foreign creditors are dealt in insolvency proceedings just like Brazilian creditors, however, its corporate documents and signatures in Brazilian documents, such as power of attorneys, must be notarised, consularised and sworn translated. Brazil has not adopted the UNCITRAL Model Law or any other treaty regarding cross-border insolvency proceedings. There are, however, provisions in Brazil that allow recognition of foreign decisions by the Superior Court of Justice, once legal requirements are fulfilled, but not recognition of processes themselves. The main requirements are:

- the decision must have been rendered by a competent court;
- the parties must have been duly summoned;
- the decision must be final, binding and unappealable and have all the requirements to be able to be enforced in the jurisdiction in which it was rendered;
- the decision must have been certified by a Brazilian consul and sworn translated; and
- the decision must be in compliance with the Brazilian public policy, sovereignty and principles of morality.

#### COMI

**48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

As already mentioned above, the competent court to ratify out-of-court reorganisation plans, grant judicial reorganisation proceedings and decree the forced liquidation of a company is the court where the main establishment of the company is located. Thus, in Brazil there is no specific concept of COMI, only a reference to 'main establishment'. When interpreting this concept, the majority of scholars and court precedents indicate that the location where the company has its registered office or major office is not important, but rather the location that concentrates the centre of management or main activities of the company. It is, therefore, an economic test.

#### Cross-border cooperation

**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

The BRL, and other Brazilian laws, do not contain any specific rules dealing with extraterritorial bankruptcy or insolvency proceedings or provisions regarding the recognition of other countries' statutory processes, unlike Chapter 15 of the US Bankruptcy Code, for example. In fact, bankruptcy and restructuring proceedings involving Brazilian companies, with their centre of main interest in Brazil, must necessarily be administered by a Brazilian court. As a result, any effects and consequences of possible ancillary or parallel proceedings in foreign jurisdictions will have to be dealt with on a case-by-case basis, subject to applicable conflicts of law provisions in cross-border matters.

#### Cross-border insolvency protocols and joint court hearings

**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

See question 49. Also, some Brazilian companies that entered into a judicial reorganisation proceeding according to Brazilian legislation have also entered into Chapter 15 in the United States, but the communication of such fact in Brazilian courts usually occurs through the debtor company itself.

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# Bulgaria

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The legislation applicable to insolvencies and reorganisations spans several acts governing the general and special procedures with regard to the type of company or enterprise concerned, for example, the Commerce Act, the Bank Insolvency Act and the Credit Institutions Act, the Insurance Code, the Social Security Code, and Council Regulation No. 1346/2000 of 29 May 2000 on insolvency proceedings. Subordinate legislation contains provisions affecting certain areas of the insolvency and reorganisation procedures in order to guarantee the receivables of employees, investors, insured persons or bank clients.

Merchants are declared insolvent due to illiquidity, which occurs when they cannot fulfil an outstanding obligation arising from a commercial transaction, public obligation arising from their commercial activity or a private obligation to the state. Corporate legal persons can also be declared insolvent if they are over-indebted – meaning that the obligations they have undertaken, although not being due, are overwhelming and cannot be covered by the short- and long-term assets of the company.

Special legislation concerning banks, insurance companies and supplementary social insurance companies states that such legal persons may enter into insolvency procedures if they lose their licence.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The competent first instance court in all insolvency procedures is the regional court where the seat of business of the merchant was located at the moment when the petition for initiation of the insolvency proceedings was submitted. The competent Court of Appeal and the Supreme Cassation Court act as a second and third instance respectively. The civil courts have exclusive jurisdiction over all matters in the insolvency procedure.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The Bulgarian state, municipalities and state enterprises exercising constitutional monopoly over certain commercial sectors, or those incorporated through a special law, cannot be declared insolvent. Banks, insurance companies and supplementary social insurance companies are subject to special rules regarding their insolvency procedures which include mandatory supervision by the Bulgarian National Bank (BNB) and the Commission for Financial Supervision (CFS).

Corporations that can be declared insolvent have all their property included in the insolvency estate. Natural persons, such as sole merchants and liable partners in partnerships, have certain properties that are excluded from the insolvency proceedings, such as their only abode, private belongings for common use, machines, books and gear used for the debtor's profession and agricultural land of up

to 30 hectares. These exceptions are only valid if the debtor has not attempted to dispose of said properties in some way.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The government-owned enterprises that exercise state monopoly over a certain commercial sector or that are incorporated through an individual law are explicitly excluded from the scope of the common rules of the insolvency proceedings under the Commerce Act. The law prescribes that all relations concerning the insolvency of such public enterprises shall be regulated in a law, specially created for this purpose. At the same time if a public enterprise does not exercise state monopoly or is not incorporated through an individual law, then it is a subject of the common insolvency procedure, applicable for all enterprises.

If a monopolistic public enterprise becomes factually insolvent, the responsible state or municipal authority shall undertake informal steps to settle its obligations towards the creditors. In case of an enterprise, created through an individual legal act, the specific rules of such law shall apply. The specific regulations which are created for the specific public enterprise shall apply to its creditors. For all other types of public enterprises the common regulations of the insolvency procedure shall apply.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

The law treats the government-owned enterprises, banks, insurance companies and supplementary social insurance companies differently – as 'too big to fail' – and has provided differently than the ordinary commercial enterprises' insolvency treatment. No insolvency proceedings can be initiated against government-owned enterprises (see question 4).

Insolvency proceedings against banks can only be initiated by BNB, while insolvency proceedings against insurance companies and supplementary social insurance companies can only be initiated by CFS, and only after their licence has been revoked.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

There are two ways to take a security over an immovable property under Bulgarian law: through mortgage over a separate property and through a special pledge over a commercial enterprise under the Special Pledge Act (SPA), wherein the entire enterprise of the debtor is pledged, including all immovable and moveable assets.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

Bulgarian law recognises common and special pledge. Under the common pledge the debtor transfers the possession over a property to the

creditor while retaining the ownership. Under the special pledge the property remains in possession of the debtor. It is typically used for personal properties necessary for the everyday business activity of the debtor.

In civil law, a creditor has the right of lien on a debtor's personal property in his or her possession only for the obligations arising from its preservation, maintenance, repair and improvement, or for damages caused by it. In commercial law, a creditor is entitled to a lien on any moveables and financial securities of the debtor, for any claims against the debtor, arising from a transaction concluded between them. Title retention over sold chattels until the price is paid in full is allowed under Bulgarian law, but in such an event the risk of damage or destruction of the property does not pass to the buyer until the ownership is transferred in full.

#### Unsecured credit

##### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Unsecured creditors may request a pre-judgment attachment over the debtor's assets by securing a present or future legal action. The procedure for securing a future claim is simple, quick and aims to surprise the debtor. The creditor must prove before the court that his or her claim has reasonable grounds and that the security measure is necessary for its satisfaction. If the court approves the petition for securing the claim, the creditor has up to one month to bring an action before it. If he or she does so, the measures remain in force for the rest of the trial. The attachment or the injunction make the creditor a joint claimant to any present or future execution over the secured property, meaning that a portion of any sums collected shall be kept for him or her until the court proceedings regarding his or her action are complete.

No special rules apply to foreign creditors.

#### Voluntary liquidations

##### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Voluntary liquidations may be commenced if the merchant has been established for a certain term – by the end of it, or by a decision of the competent management body. When the procedure is initiated, the legal entity ceases all its business activity. A liquidator who represents the enterprise is appointed by the competent body of the merchant. He or she observes and manages the termination of the company by fulfilling the remaining obligations, claiming all receivables, drawing an inventory of all assets, determining and distributing the liquidation shares between the shareholders.

A voluntary liquidation may be carried out only if the enterprise of the merchant has enough assets to cover all its outstanding obligations. If the liquidator discovers that the company is in a state of illiquidity or over-indebtedness, he or she is obliged by law to initiate an insolvency procedure.

#### Involuntary liquidations

##### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Involuntary liquidations are not regulated separately under Bulgarian law. They find their place somewhere between the voluntary liquidation, whereas they bear resemblance in the fact that the merchant's enterprise must still have enough assets to cover all outstanding obligations, and insolvency procedures since they are usually initiated by the court or government authority against the merchant's will.

Common corporate legal persons or partnerships may enter involuntary liquidation procedure if they are terminated by the court due to irregularities in their registration or non-compliance with mandatory provisions of the law for their existence, if an action is brought by a prosecutor or an interested party. The procedure and its prerequisites are the same as those in voluntary liquidations. The legal entity ceases all business activity and initiates cash down procedure.

#### Voluntary reorganisations

##### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The debtor, the insolvency administrator, part of the creditors, part of the shareholders, the partners with unlimited liability and 20 per cent of the employees of the debtor can all offer a reorganisation plan in the general insolvency proceedings within a month of the court's decision approving the lists of accepted claims.

The law allows the debtor to settle his or her obligations out of court via contract with all creditors, which, after being concluded, must be presented before the court.

The major effect of such reorganisation is that the insolvency proceedings are stayed and a procedure for the merchant's recovery is initiated.

#### Involuntary reorganisations

##### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Only creditors with more than one-third of secured or unsecured claims are entitled to offer a reorganisation plan in the insolvency proceedings. The approval of the debtor is not required and the law obliges him or her to comply with it even if he or she has not agreed to the reorganisation.

#### Mandatory commencement of insolvency proceedings

##### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

A debtor who has become insolvent due to illiquidity or over-indebtedness is obliged to file a petition for the commencement of an insolvency procedure before the regional court within 30 days from the date of factual insolvency. The petition is filed by the debtor, his or her heir, a management body, a representative or a liquidator of the company, or by a liable partner. The non-fulfilment of this obligation leads to joint and several liabilities of the above-mentioned individuals along with the insolvent merchant before the company's creditors for any damages caused.

Furthermore, the infringement of these obligations may lead to criminal liability of the person entitled with the obligation to file the petition, as the Bulgarian Criminal Code envisions an imprisonment of up to three years or a fine of up to 5,000 Bulgarian leva. In the event that a merchant carries on its business while insolvent without filing a petition, some of its transactions may be invalidated.

#### Doing business in reorganisations

##### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

During initiated insolvency proceedings, the debtor may carry on its business under the supervision of the insolvency administrator. The debtor may perform new transactions only with the prior approval of the insolvency administrator. If the debtor endangers the interests of the creditors, the court may deprive him or her of the right to manage and dispose of his or her assets.

If creditors have receivables that have occurred after the date of the court's decision on the insolvency proceedings, they receive their payments on the due date or are satisfied preferentially before unsecured claims pursuant to the specific order of claims under the acting legislation before unsecured ones.

The creditors with approved claims form the meeting of creditors and the optional creditors' committee (see question 28) that oversee the debtor's ongoing business activity and elect an insolvency administrator who approves any transactions or contracts made by the debtor.

The court initiates and terminates the insolvency proceedings, supervises the debtor's activity and has the powers to declare transactions invalid in respect to the insolvency creditors on specific grounds provided by the legislation.

If a recovery plan has been approved by the meeting of creditors and affirmed by the court, all business transactions of the insolvent enterprise are carried out under the supervision of a supervisory body, determined and appointed by the creditors and approved by the court.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

All judicial and arbitration proceedings on civil and commercial cases brought against the debtor are stayed upon the start of the insolvency proceedings except the labour court proceedings for monetary receivables of employees of the debtor. On the other hand, in the case of initiated liquidation procedure all the legal proceedings continue normally.

The prohibition itself shall not be applied if, up until the date of when the insolvency proceedings have been initiated, there is another case in which the debtor is a defendant and the court has admitted for joint hearing a counter claim or a set-off objection made by the debtor. Certain creditors may also obtain a relief from this prohibition in the event of claims for monetary receivables secured by a property owned by third parties.

The enforcement proceedings for any properties included in the insolvency estate, with the exception of the secured public receivables, are stayed as well.

Bringing a new court or arbitration proceedings for civil or commercial cases against the debtor is not allowed with the exception of claims for the protection of third-party rights on properties included in the insolvency estate, labour disputes and monetary receivables secured by property owned by third parties.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Bulgarian law does not explicitly prohibit the obtaining of secured or unsecured loans or credits by a debtor during the insolvency proceedings. However, such a transaction is performed under the supervision of the insolvency administrator who must approve the deal, especially if the loan, respectively the credit, will be secured with a property from the insolvency estate.

Despite the fact that the receivables on the loan or the credit have emerged after the date of the decision for initiation of the insolvency, the creditors have the right to receive payment on the due date. If such a payment is not received, they are satisfied preferentially from the insolvency estate before the unsecured creditors but after secured ones.

In the liquidation proceedings the merchant could obtain a loan or credit only if this is needed for performing the liquidation, but such case is rare.

### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

The legislation allows a creditor to effect a set-off with his or her debt towards the debtor in the initiated insolvency proceedings if prior to the insolvency both of the debts have existed and are mutual, of the same kind and the creditor's claim is due.

The CA prescribes that all monetary and non-monetary obligations of the debtor become due as from the date of the court's decision for declaring the insolvency. If the creditor's claim has become due in the course of the insolvency proceedings or as a result of the court's

decision, as well as if both of the debts have become of the same kind, the creditor may effect a set-off after the claim has become due or, respectively, uniform. In both cases the statement for the set-off shall be made before the insolvency administrator.

The set-off may be declared void in respect to the insolvency creditors if the creditor has acquired the claim and the debt towards the debtor before the decision for the initiation of the insolvency, if he or she has known that the debtor is insolvent, respectively over-indebted, or that a petition for the initiation of the insolvency proceedings was filed before the court.

### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

In the insolvency proceedings, which include both reorganisation and liquidation, Bulgarian legislation allows several cases of sale of assets of an insolvent debtor: special cases of sale of specific assets by the insolvency administrator by means of direct negotiation; sale of the enterprise of the insolvent merchant or a part of it; and sales of the assets of the debtor through an auction. These sales are implemented by the insolvency administrator with the prior permission of the court. The purchaser acquires the assets 'free and clear' of claims, as the creditors having securities on them are being satisfied in a specific order.

Bulgarian law does not regulate a sale under the 'stalking horse' bids manner as the sales in the insolvency procedure may be implemented only through an auction or direct negotiations. As far as how the sales and their conditions are implemented by the insolvency administrator after the approval of the creditors' assembly and the court, there are no 'stalking horse' bids in the sale procedure. All of the proposed bids are listed by the insolvency administrator who sells the relevant asset to the purchaser who has offered the highest price.

Bulgarian practice is unfamiliar with the legal figure of credit bidding. The purchase of assets by a creditor has not been explicitly forbidden by the law, but it should be taken into consideration that all of the amounts raised by the performed sale of assets are collected by the insolvency administrator and distributed to all of the debtor's creditors.

The court does not consider any specific factors during the assessment of any bid. It only approves the sale executed at auction and managed by the insolvency administrator. The law does not prevent the assignee of the original secured creditor to participate in the auction. The only restrictions are for the debtor, its representative, the insolvency administrator, the persons who manage or guard the property, judges, prosecutors, state and private bailiffs, entry judges and lawyers – who shall not have the right to participate in the bidding.

### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

There are no specific rules regulating the legal status of a licensing agreement if an insolvency procedure has been opened against the debtor. The termination of the relationships between the licensor and the licensee is a manner of specific arrangement in the concluded agreement. Opening a procedure of insolvency upon the licensee may be set as a condition for the termination of the agreement.

On the other hand, the intellectual property itself is a part of the insolvency estate in the event of insolvency instituted against the licensor and can be sold or transferred under the supervision of the insolvency administrator and the court. The insolvency administrator may continue using the IP rights only if he or she has reached an agreement with the licensor.

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**Personal data in insolvencies**


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**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Bulgarian legislation provides restrictions on the use of personal data related to the insolvency proceeding. Pursuant to the legal requirements 'personal data' shall refer to any information related to an individual who is identified or identifiable, directly or indirectly, by reference to an identification number or to one or more specific features. The actual legislation prescribes the personal data to be processed in legal compliance and in a bona fide manner; collected for specific, precisely defined and legal purposes and not be submitted to additional processing in a manner incompatible with such purposes; proportionate to the purposes for which they are being processed and not exceeding their scope.

Personal data may be processed only in cases when at least one of the following conditions is met: the processing is necessary for the execution of an obligation of the personal data controller, stipulated by law; the individual to whom such data refer has given his or her explicit consent; processing is necessary for the execution of obligations of a contract to which the individual to whom such data refer is a party, and for actions at the individual's request and preceding the execution of a contract; the processing is necessary in order to protect the life and health of the individual to whom such data refer; the processing is necessary for the performance of a task carried out in the public interest; the processing is necessary for the execution of competences vested by law in the data controller or in a third party to whom the data are disclosed; the processing is necessary for the execution of the legitimate interests of the personal data controller or a third party to whom the data are disclosed, except where such interests have priority over the interests of the individual to whom such data refer.

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**Rejection and disclaimer of contracts in reorganisations**


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**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

The insolvency administrator is entitled by means of written notification to terminate any contract to which the debtor is a party, in case it has not been performed wholly or partially. In this case the other party is entitled to receive a compensation for any damages incurred.

If an insolvent debtor breaches a contract after the insolvency case is opened, the relevant damages occurred for his or her creditor may be filed as unsecured insolvency claims, except for the agreements secured before the start of the insolvency proceedings.

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**Arbitration processes in insolvency cases**


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**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

The Bulgarian court has the sole and exclusive jurisdiction to review insolvency cases. The legislation does not allow arbitration concerning the insolvency proceedings.

Arbitration proceedings cannot be continued after the insolvency procedure is opened since the law prescribes that all judicial and arbitration proceedings on civil and commercial cases brought against the debtor with regards to his or her property must be stayed upon the initiation of the insolvency proceedings, with the exception of the labour court proceedings for monetary receivables, which are not subject to arbitration under Bulgarian law.

After opening the insolvency proceedings it is unacceptable for new civil or arbitral proceeding to be initiated except for those that are related to labour disputes or affect right of third parties who own

property included in the insolvency estate or to monetary receivables, secured by third party's property.

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**Successful reorganisations**


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**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

The reorganisation plan may provide a rescheduling of payments, a release from liability in full or in part, a reorganisation of the enterprise, or the undertaking of other acts, transactions or measures. The mandatory contents are:

- extent of fulfilment of the claims, the manner of satisfaction of the creditors and the relevant time period for it, the guarantees for the objected or denied claims;
- terms and conditions under which the partners are released from liability;
- extent of satisfaction received by each class of creditors;
- guarantees provided to each class of creditors;
- managerial, organisational, legal, financial, technical, and other actions for the implementation of the plan; and
- influence of the plan on the employment of the debtor's employees.

The meeting of creditors is entitled to approve the plan. The voting is conducted in separate classes. The plan must be adopted by the creditors of each class by a simple majority. Afterwards the court approves the proposed reorganisation plan if it complies with the law.

The release of non-debtor parties from liability is a mandatory part of the plan as well and the CA does not prescribe specific conditions for the release. The release from liability comes into force after with the affirmation of the plan by the court.

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**Expedited reorganisations**


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**24 Do procedures exist for expedited reorganisations?**

Bulgarian legislation does not provide a specific expedited procedure for the reorganisation of an insolvent merchant. Nevertheless, the CA prescribes that a reorganisation plan may be proposed at different stages of the insolvency proceedings, but no later than one month from the registration of the court's ruling that approves the list of creditors with admitted claims in the Commercial Register.

A reorganisation plan may be proposed at the very beginning of the insolvency process, together with the submission of the petition for initiation of the insolvency by the debtor or by a creditor, which may expedite the reorganisation proceedings in respect of the time needed for the entire recovery procedure.

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**Unsuccessful reorganisations**


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**25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

If a plan is rejected, a reorganisation process cannot be held. There are several ways for this to happen: the court may refuse to admit it for review by the meeting of creditors; the meeting of creditors may reject the plan by voting against it; or the court may refuse to approve the plan due to non-compliance with the regulations for its approval.

If the debtor fails to implement the adopted plan and its obligations, the creditors or the supervisory body may request the reopening of the insolvency procedure. In such cases illiquidity or over-indebtedness are not proved again and the transformative effect of the plan concerning the creditors' rights remains unchanged. Another legal consequence is that no reorganisation plan can be introduced again in the reopened insolvency procedure.

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**Insolvency processes**

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

All creditors receive notices for an appointed meeting through an invitation, given by the court and published in the Commercial Register. The creditors who are involved in litigation regarding their claims receive summons at their appointed address in the country. Creditors domiciled abroad without address in Bulgaria must appoint a legal address in the country.

The actions of the debtor, the creditors, the creditors' committee, the meeting of creditors, the insolvency administrator, as well as the acts of the court are registered into a special journal that is publicly available at the office of the insolvency court. The decisions of the appellate and cassation court on appeals against the acts of the regional court are made available to the persons concerned via written summon.

The insolvency administrator submits a report of his or her activity to the court and the creditors each month, or when asked. At the request of a creditor, the insolvency administrator shall present to the latter the logbook, the report and also an answer to any particular issues if they have not been answered in the report for the same period. The insolvency administrator is obliged to submit a final report at the conclusion of his or her work, which the creditors may raise objections to.

In general, the creditors may not pursue the estate's remedies against third parties because after the insolvency process is opened this is one of the insolvency administrator's powers. However, in regard to invalidation claims (see question 37), if the administrator fails to exercise his or her powers on the matter, the creditors may act instead.

The liabilities of all third parties, outside the debtor's group, cannot be released. The alleviations foreseen in the reorganisation do not apply to third parties, liable for the debtor's obligations. The law provides that the plan is mandatory for the debtor and the creditors. It is explicitly prescribed that guarantors, persons who have arranged a pledge or a mortgage for securing debtor's obligations, and persons liable jointly and severally with the debtor, cannot use the reliefs of the plan.

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**Enforcement of estate's rights**

**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

If the available assets of the debtor are not sufficient to cover the insolvency proceedings expenses (including for pursuing a claim), the court shall determine an amount to be paid in a set period by the creditors. The other option is the court to allow the compulsory sale of insolvency assets. However, the creditors cannot pursue the claims themselves, unless the insolvency administrator refuses to act himself or herself (see question 25) except for the invalidation claims (see question 39).

Any fruits acquired from the remedies regardless of the person who has led the collection belong to the insolvency estate and are distributed under the order of claims prescribed by the CA.

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**Creditor representation**

**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

The most significant committee is the meeting of creditors. Only creditors whose claims have been admitted by the court have voting rights at the meeting. The meeting has the power and obligation to elect and dismiss the insolvency administrator, to determine his or her remuneration, to hear his or her reports; to elect a creditors' committee and change its members, to hear the report of the creditors' committee, to determine the order and the way of conversion of the debtor's property, the method and the terms for evaluation of the property, etc.

The other representative body of the creditors is the creditors' committee. The election of this committee is optional. It assists and supervises the activities of the insolvency administrator, inspects the

commercial accounts and cash availabilities and may also give an opinion regarding the continuation of the activity of the debtor's undertaking, the activities related to the conversion in cash and the liability of the insolvency administrator.

The creditors may elect a supervisory body together with the adoption of the recovery plan. It supervises the performance of the plan, hears reports on the merchants activity, gives prior approval to legal acts having effect on the debtor or on his or her long term business activity and proposes reopening of the insolvency procedure.

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**Insolvency of corporate groups**

**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

Bulgarian legislation does not provide special rules for insolvency proceedings involving corporate groups. In relation to companies forming a corporate group, the proceedings are initiated separately for each company of the group. The insolvency procedure shall proceed separately even though it was initiated for two or more companies, who are a part of the group. The competent court is entitled to resolve on each company of the group whether it meets the requirements of the law regarding declaring it insolvent. The assets may not be transferred from an administration in Bulgaria to administration in another country, the court remains the sole organ authorised to supervise and lead the insolvency proceedings.

Since the companies from a group are united on the basis of capital participation from one company to another, it is most likely (based on economic criteria) that when one or some of the companies of the group are facing liquidity the other companies will also be at risk of insolvency. The risk is higher for the subsidiaries when the parent company is bankrupt.

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**Appeals**

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

According to the actual Bulgarian legislation, the appellant does not have to obtain a permission to appeal the relevant court order in the insolvency proceeding as far the appellant is an interested party.

Bulgarian legislation provides special rules for the term within which a court order may be appealed.

For example, the court order with which it is decided an insolvency proceeding to be opened or rejected may be appealed within a seven-day term as from the date of its announcement in the Commercial Register.

The actual legislation does not provide requirements for posting a security in order to appeal a court decision by the relevant interested party.

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**Claims**

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

The creditors are given three-month terms counted as from the publication of the decision for initiation of the insolvency proceedings in the Commercial Register to submit their claims in writing before the insolvency court. After that no claims that have emerged before the date of initiation of the insolvency proceedings may be submitted.

The insolvency administrator draws up a list of submitted claims, a list of the claims of employees and a list of denied claims. A creditor may object any claim admitted or rejected by the insolvency administrator. Otherwise the court approves the list of admitted and officially entered claims. If there are objections, the court examines them and

calls all creditors to a meeting of creditors where all objections are examined. If they are found to be justified the court may modify the list. The court adopts the final lists with a ruling that is not subject to appeal.

There are no provisions set out in legislation on the transfer of claims in the insolvency proceedings; respectively there are no restrictions or an obligation to disclose the transfer of claims.

A claim under a postponing condition is included in the initial distribution as a disputed claim. An adequate distribution amount is set aside for it. In the final distribution, this claim shall be excluded in case the condition has not occurred. A claim under a terminating (peremptory) condition shall be included in the distribution as unconditional. If the condition takes place during the insolvency process the claim shall be terminated but if the condition occurs before the final distribution of the estate the sums paid to the creditor shall not be returned. The remaining part of the claim is terminated as a result of the peremptory condition's occurrence.

There are no legal obstructions for a claim acquired at a discount to be enforced in full.

Any interest that accrued after the opening of an insolvency case could be claimed by a creditor but if the interest is on non-secured claims it shall be satisfied following the complete satisfaction of the rest of the creditors.

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### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The court cannot change the rank given to the claims by the law. The court could change the rank as defined by the creditor in its application for a claimed receivable. After the insolvency administrator registers the receivables in the lists of claimed receivables each creditor is entitled to object such claim and the given rank. The insolvency court calls a hearing where discusses all objections and takes in consideration all given evidence. Depending on the evidence the court could change the rank of a claimed receivable (eg, from secured to unsecured). Such a procedure is common and occurs often, almost in all insolvency proceedings.

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### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

The creditors in the insolvency process may be divided into three categories according to the type of their claims: secured, unsecured and creditors whose claims are satisfied following the full satisfaction of the rest of the creditors. All claims are arranged in rows in accordance with the order of claims prescribed by the law.

In the group of secured claims the major privileged ones are claims secured by a pledge or mortgage and the claims against which a right of lien is exercised. The secured claims are satisfied by the realisation of the security.

The claims for insolvency expenses, claims arising from employment relations that have emerged before the date of the decision for initiation of the insolvency proceedings, maintenance owed by the debtor to third persons and public claims of the state such as taxes may have priority over secured claims only if the secured claims have emerged after the date of the decision for initiation of the insolvency proceedings and are not paid on the due date.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

The employment contracts may be terminated by the employer with a notice period of one month when the employer ceases its business activity. The employment relationship does not terminate during a restructuring of the employer. In the event of enterprise transfer (eg, as a part of restructuring plan) the rights and obligations of the employer before the change are sustained with the new owner of the enterprise. The liability of the employers may be joint or several, depending on the type of restructuring.

The claims of employees which have emerged before the date of the court's decision for the initiation of the insolvency proceedings are ranked fourth in the order of claims.

The Act on Guaranteed Claims of Employees in the Event of the Employer's Insolvency governs conditions under which the employees' claims arise after lay-offs due to insolvency and the amount of claims guaranteed by a special fund established under the act. The employees' claims are guaranteed for an amount of up to six monthly salaries left unpaid in the 12 months prior to the termination of the employment contract. The claims of employees that are not guaranteed by the fund can be brought in the insolvency proceedings and would be in the seventh row in the order of claims.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

State claims for mandatory social security contributions of the employer for pension funds are satisfied preferentially on the sixth row in the order of claims prescribed by the CA.

However, the pension claims are in general secured by the guarantee fund, mentioned in question 34. Along with the payment of guaranteed claims of the employees', the employer pension contributions due (for the state public insurance) and the health-care contributions are also paid by the guarantee fund in the event of employer insolvency.

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Bulgarian legislation does not set out any provisions concerning cases in which there are environmental problems in insolvency proceedings. As long as the debtor still operates, he or she, as a legal entity, is responsible for any damages caused. The insolvency administrator, creditors, the debtor's officers and directors, or third parties bear no liabilities on behalf of the insolvency estate unless caused by their own fault. If assets are insufficient to prevent any arising problems, municipal authorities bear responsibility for their prevention.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Unsatisfied liabilities may be restored if within a year of an insolvency termination amounts set aside for disputed claims are released or new assets discovered. The proceedings are resumed after a written request of a debtor, creditor or after confirmation by a court decision in a separate litigation.

With reorganisation plans, debts only survive the termination of the insolvency proceedings if and to the extent they are specified in the reorganisation plan as it may provide for a deferment or rescheduling of payments. If the debtor does not perform his or her obligations under the plan, the creditors whose claims have been transformed by the plan may request the resumption of the insolvency proceedings. The liabilities of the debtor survive in the new insolvency proceedings, but the transformative effect of the plan concerning the creditors' rights and the remedies is preserved.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

The distribution of the amounts, collected after the compulsory sale of assets, is carried out when sufficient cash funds have been accumulated in the insolvency estate. The insolvency administrator drafts a bill for the distribution of the available amounts among the creditors with admitted claims in conformity with the order, the privileges and the remedies prescribed by the law. The distribution bill is considered

### Update and trends

The legal system of Bulgaria is in a continuous process of aligning itself with the European Union's and the world's standards in insolvency proceedings and constituting a legal practice in accordance with European Union legislation, ensuring equal rights and possibilities for both Bulgarian and foreign creditors and debtors in insolvency proceedings.

partial until the debts have been paid in full or the entire insolvency estate (except the objects deemed unsellable) has been converted into cash.

The final distribution is carried out after the insolvency court approves the distribution account. The insolvency court can make changes to the distribution bill if there are defects established ex officio or following an objection for non-compliance with mandatory provisions of the law. The approved bill is then published in the Commercial Register and is executed by the insolvency administrator. Distributions pursuant to a reorganisation plan are not restricted by the terms of the CA and, therefore, payments to creditors should be consistent with what has been agreed between them in the plan.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

Once insolvency proceedings have been commenced and reach the phase of constitution of the insolvency estate, some transactions or actions of the debtor may be considered void by law in respect to the creditors, and others may be revoked in a further litigation led by the insolvency administrator, or by the creditors if he or she refuses to exercise his or her rights on the matter. In general all actions and transactions harm the amount of the insolvency estate by decreasing it (eg, performance of a debt that has emerged prior to the date of the decision for initiation of the insolvency proceedings or arrangement of a pledge or a mortgage on rights or objects included in the insolvency estate, etc).

The activities and transactions subject of annulment should be carried out by the debtor within the period from the initial date of the illiquidity, respectively, the over-indebtedness to the date of the petition for opening of insolvency proceedings.

Another group of for acts and transactions could be annulled if they harm the insolvency estate and are performed after the date of submission of the petition for initiation of insolvency proceedings.

An action for invalidation must be brought before the court and if successful, the act or transaction is annulled in respect to the creditors.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The period between the initial date of illiquidity or over-indebtedness, determined by the insolvency court, and the submission date of the petition for initiation of the insolvency proceedings is known in the legal doctrine as the 'suspect period'. A series of legal transactions committed by the debtor in this period can be revoked by law or by the insolvency administrator through an action brought before the competent court. Should he or she fail to do so, any insolvency creditor can exercise this power within one year following the initiation of proceedings. When the claim is brought by a creditor, the court shall constitute the administrator in the insolvency proceedings as a joint applicant ex officio.

The suspect period for the invalidation claims set out in article 647, CA is calculated differently. Here the date of illiquidity or over-indebtedness is not a constituent element. Instead, the suspect period for these types of claims begins from the submission date of the petition for initiation of insolvency proceedings.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

In principle, the corporate officers and directors are not liable to third parties for obligations owed by the companies they represent. Only the company can be held liable for their actions. Personal liability of a manager or a management board member can only arise in a few exceptional cases specifically listed in the Commerce Act.

The corporate officers and directors are liable for any damages caused to the company through a fault.

Failure to comply with the obligation of filing a petition for initiation of insolvency proceedings leads to joint and several liability of the representatives with the debtor company before the creditors for any damages caused and a criminal liability (see question 13). Intentionally conducting a business activity in a way leading to insolvency is also a crime under the Criminal Code. Many actions of the merchant or his or her competent bodies in the insolvency procedure can also lead to criminal liability if done intentionally: concealing assets of the company, concluding further contracts or transaction while knowing that their performance is impossible, sabotaging reorganisation plans, violating the order of claims, hiding or destroying accounting books, etc.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Bulgarian legislation does not contain any special rules about the parent company or affiliated company's responsibility for the liabilities of subsidiaries and insolvency proceedings involving corporate groups. In principle, neither the parent nor the affiliated companies can be held liable for the obligation of subsidiaries or affiliates. The respective entity could be responsible on the grounds of an agreement (guarantee, warranty, etc), signed with its affiliate or subsidiary. There are no specific rules for pro rata distribution of group company assets. The law foresees individual court proceedings for each debtor. In case of insolvency of a group of companies each company of the group is a subject of a separate court proceedings. The court is not able to decide on the assets of a debtor from the group which is not subject of the process, led by the same judge.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Specific restrictions can be found in the Act on Guaranteed Claims of Workers and Employees in the Event of Employer's Insolvency. The guaranteed amount of the receivables, ensuing from employment relations, are not paid to employees who, on the initial date of insolvency, have been partners in the merchant company, members of the managing or supervisory boards of the merchant or are spouses or relatives of the entrepreneur, or of the persons under the previous two items.

Under the BIA, members of the managing board, people working for the Bank Claims Guarantee Fund, cannot acquire in any way whatsoever, directly or through another person, a possession or a right of the bank's insolvency estate. This restriction also applies to the spouses and relatives of such persons.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

The Special Pledge Act allows the creditor to enforce his or her claims out of court among properties secured by a special pledge. The secured creditor may file for enforcement and appoint a special enforcement officer (depository) who commences the compulsory sale procedure. The compulsory sale itself is carried out by the secured creditor with due diligence, but any amounts collected are paid to the depository.

The depository draws up a distribution bill and notifies all creditors and the debtor. The bill can be appealed before the district court. The

amounts are distributed in a specific order specified by the law. If any amounts remain after the distribution, they are returned to the debtor.

The initiation of the insolvency proceedings cannot interfere with this type of enforcement.

#### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Voluntary liquidation procedures specified in question 9 apply to corporate legal persons. The general meeting of shareholders has the right to terminate the company. Majority or quorum requirements that differ from those in law may be set in the articles of association.

The resolution for termination is published in the Commercial Register along with the appointed liquidators and invitation to all creditors. The liquidator supervises and manages the termination of the company.

In contrast to insolvency proceedings, voluntary corporate liquidation usually takes place without the intervention of the court, since the company has enough assets to satisfy all outstanding claims. The debtor remains in control of the company through the appointed liquidator. Compulsory sales cannot be enforced by creditors and the liquidator is free to choose the method of asset liquidation. If any amounts remain after all creditors have received satisfaction, they are distributed between shareholders as liquidation shares.

#### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

The liquidation and the reorganisation cases are formally concluded by a judicial act of a relevant authority.

In voluntary liquidation, a corporation is considered dissolved when the Commercial Register enters it in the company file.

In general, the insolvency procedure is terminated by a court's decision if the debts have been paid, a reorganisation plan or out-of-court settlement have been adopted or when the insolvency estate has been depleted. In the event of the latter the merchant is deleted from all registers.

#### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

As an EU member state, the relations regarding the cross-border insolvency proceedings in Bulgaria are regulated under the European law such as Council Regulation (EC) No. 1346/2000 of 29 May 2000 on insolvency proceedings.

As soon as insolvency proceedings are opened in a member state, the competent court or the appointed liquidator will immediately notify known creditors who have their habitual residences, domiciles or registered offices in other member states.

According to the Regulation, the law of the state where the proceedings are initiated governs the conditions for their initiation, conduct, closure and creditor claims.

On conditions of reciprocity Bulgaria may recognise foreign judicial decisions that declare insolvency, provided they are passed by an authority of the state of the debtor's domicile. At the request of the debtor, insolvency administrator or a creditor, a Bulgarian court may institute subsidiary bankruptcy proceedings in respect of a merchant who has been declared bankrupt by a foreign court, in respect to the debtor's substantial assets in the country.

#### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

As an EU member state, Bulgaria determines the COMI under the Regulation (EC) No. 1346/2000, according to which the COMI should correspond to the place where the debtor conducts the administration of his or her interests on a regular basis and is therefore ascertainable by third parties. In the case of a company or legal person, the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary. The location of the COMI determines the court competent to initiate the insolvency proceedings.

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**Cross-border cooperation**


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**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

The CA allows for a foreign (non-EU) competent court's decision to be admitted for execution provided there is a mutual agreement of reciprocity between the Bulgarian state and the state where the court issuing the decision on the insolvency is situated. A foreign insolvency administrator may legally exercise his or her powers under the foreign legislation in Bulgaria insofar as they are not in variance with the public order in Bulgaria (meaning they should not be in violation of human rights and the moral principles of Bulgarian and European society).

The acting legislation allows for a secondary insolvency procedure to be initiated in Bulgaria at the request of a foreign insolvency administrator, debtor or creditor to the Bulgarian court.

Bulgarian courts have the right to refuse to recognise foreign insolvency proceedings if they originate from a non-EU country that has no mutual agreement with Bulgaria on the matter, or if the decision of the foreign court or measures prescribed contradict the established public policy in the country.

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**Cross-border insolvency protocols and joint court hearings**


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**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

Bulgarian courts have still not held joint hearings with courts in other countries or entered into cross-border insolvency protocols. Subsidiary insolvency proceedings have been initiated in regard to a foreign debtor's assets in the country as per Regulation (EC) No. 1346/2000.

# Canada

Bruce Leonard Chair, The International Insolvency Institute

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

Bankruptcy liquidations are governed by the Bankruptcy and Insolvency Act (BIA). Restructuring proceedings may be initiated under the BIA or the Companies' Creditors Arrangement Act (CCAA), both of which are federal legislation. The BIA provides for both reorganisations and liquidations of insolvent businesses and individuals. The CCAA provides for only reorganisations or liquidations of corporate entities, although the courts frequently authorise significant asset sales in CCAA proceedings. The CCAA applies to a company or an affiliated group of companies with liabilities in excess of C\$5 million.

A debtor is considered insolvent if it is unable to meet obligations as they become due; it has ceased paying its current obligations as they become due; or the aggregate of its property, if disposed of at a fairly conducted sale under legal process, would not be sufficient to pay its obligations. These three tests are alternatives and it is sufficient to show that any one of them has been satisfied.

Where complex or fundamental changes must be made to the shareholdings and debt structures of corporations, the 'arrangement' provisions of the Canada Business Corporations Act (CBCA) and comparable provincial legislation may be applicable. CBCA corporate reorganisations can include amalgamations, liquidations, dissolutions or a combination of any of these. Occasionally, 'arrangement' proceedings are used in conjunction with reorganisations under the BIA or the CCAA.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Under federal bankruptcy law, the Superior Court in each of Canada's 10 provinces has jurisdiction over bankruptcy matters. There is no formal, separately established bankruptcy court. Superior court judges in the common law jurisdiction provinces are considered to have an inherent jurisdiction to deal with matters, even if there are no specific statutory provisions dealing with a particular matter.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Federally incorporated banks and insurance companies are excluded from the BIA and CCAA and are dealt with under the Federal Winding-up and Restructuring Act (WURA). The BIA also excludes railways, savings banks, insurance companies and trust and loan companies. Upon bankruptcy, the debtor's property vests in the trustee in bankruptcy with certain exceptions. Property owned by third parties or held in trust by the debtor for third parties does not vest in the trustee. Certain types of property are exempt by provincial and federal statutes from claims of creditors (eg, pension benefits, retirement plans and household goods).

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The Canadian experience is limited in this regard. Although there are no specific provisions in the BIA, WURA or CCAA pertaining to government-owned enterprises, there is some limited case law in which Canadian courts have held that bankruptcy legislation is not applicable to government-owned enterprises such as cities and school corporations. In some cases, government-owned enterprises are specifically prohibited from initiating formal insolvency proceedings by legislation. In addition, legislative reforms have imposed strict borrowing limits and regulatory oversight upon such entities as safeguards against default. Where the potential for default is significant, the provincial or federal government has the power to intervene and assume control of the defaulting entity.

The pursuit of contractual claims can be complicated depending on the nature of the government-owned enterprise. For instance, although creditors are generally able to initiate court proceedings against a government-owned enterprise, prior to doing so, they must deliver formal written notice to the government entity setting out particulars of the proposed claim within a prescribed period of time otherwise risk having the court proceedings dismissed. Another consideration is determining the level of court, either federal or provincial, in which the claim against the government-owned enterprise can be commenced.

## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Several of Canada's largest banks have been designated as 'too big to fail' by the federal regulator, the Office of the Superintendent of Financial Institutions. The designation stems from the framework issued by the Basel Committee on Banking Oversight and means that such financial institutions are subject to increased capital requirements and supervision. The measures are designed to limit the likelihood that a major bank failure would negatively affect the Canadian economy.

## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

Security on immovable property is usually taken in the form of a 'mortgage' or 'charge' that is registered in the Land Registry Office in the province in which the real property is located. Upon default, the secured party can usually choose between selling the property and claiming any deficiency in the amount owing from the debtor, or obtaining title in court proceedings to retain the property as its own, in which case its claims against the owner are extinguished.

## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

Security interests in moveable property are dealt with on a province-by-province basis under provincial personal property security legislation in

Canada's common law provinces. This legislation provides the requirements for taking 'security interests' in 'personal property' through the mechanism of 'security agreements'. It also prescribes conditions for enforcing security interests and the ranking of competing security interests. Finance leases of moveables are generally considered to be security interests and, in many provinces, leases of moveables for terms exceeding a year must be registered as security interests. Non-possessory security interests usually require registration in the general public registration system.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

In the absence of formal insolvency proceedings, an unsecured creditor must first prove its debt through proceedings in court. Once a judgment is obtained, assets of the debtor (including amounts owing to the debtor) may be seized and sold by a court officer, through a variety of mechanisms, to satisfy the judgment. The proceeds are distributed pro rata among all creditors holding judgments against the debtor in the locality in which the seizure took place. These remedies are not difficult or time-consuming unless the legal proceedings are defended. Although somewhat uncommon, pre-judgment attachments may be available in some provinces prior to judgment being recovered by the creditor. A creditor may also be able to obtain one of several types of temporary orders that have the effect of freezing or tying up personal or real property pending a court hearing on the creditor's claims against it.

There is no distinction between foreign and domestic creditors, except that a foreign plaintiff may be required to pay money into court as security for the legal costs of the defendant if the defendant is successful in having the creditor's claim dismissed because of the 'loser pays' rule in Canadian litigation.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A voluntary liquidation under the BIA commences when a debtor files an assignment in bankruptcy with the government bankruptcy office, accompanied by a sworn statement listing its assets and obligations. All of the debtor's unencumbered assets vest in its bankruptcy trustee, subject to the rights of the debtor's secured creditors to deal with their collateral. Unsecured creditors' remedies against the debtor's assets are stayed, but there is only a very limited stay against proceedings by secured creditors.

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

A creditor can initiate involuntary liquidation proceedings in respect to a debtor under the BIA if the creditor has an unsecured claim of at least C\$1,000. To obtain a bankruptcy order, the creditor must establish that the debtor is insolvent and has committed an 'act of bankruptcy' within the six months preceding the commencement of the case. The most common 'act of bankruptcy' is failing to meet liabilities generally as they become due. A debtor can also be placed in liquidation under the BIA if its proposal (see question 11) is rejected by its unsecured creditors or is not approved by the court, or if certain filing deadlines are not met. The practical effect of a liquidation is the same whether it is commenced voluntarily or involuntarily.

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### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Voluntary reorganisations under the BIA are commenced by either filing a proposal (which constitutes the debtor's reorganisation plan) or by filing a notice of intention to file a proposal. In either filing, an automatic comprehensive stay of proceedings is invoked, which remains in place until the debtor successfully completes its reorganisation or its reorganisation fails. Where a notice of intention is filed, the debtor

must file cash-flow statements for its business within 10 days and must file its proposal within 30 days. The court can extend the time for filing a proposal (provided that the debtor is proceeding with diligence and in good faith) for up to a maximum of six months, although it can only grant extensions for up to 45 days at a time. The debtor normally carries on its business in the normal course, subject to review by the proposal trustee and the supervision of the court.

To commence a voluntary reorganisation under the CCAA, a debtor must make an application to the court for reorganisational protection under the CCAA. In granting relief to a reorganising debtor, a Canadian court will routinely grant a very comprehensive stay of proceedings against actions by creditors while the debtor's plan is being negotiated and developed. If relief under the CCAA is granted, the court appoints a 'monitor' as an independent court officer to look after the interests of the creditors generally and to report to the court and to the creditors on the debtor's progress with its reorganisation.

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### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Under the BIA, a receiver or bankruptcy trustee can commence an involuntary reorganisation on behalf of the debtor over which it has been appointed. Involuntary BIA reorganisations commenced by creditors are rare. Creditors can commence involuntary reorganisations under the CCAA, but these are also very infrequent.

The stays of proceedings against actions by creditors in involuntary reorganisations are comparable to those in voluntary reorganisations. In voluntary reorganisations, however, the debtor is more likely to be able to create a broader reorganisational framework of protective court orders than a creditor could obtain in an involuntary reorganisation that is being resisted by the debtor.

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

There are no specific legislative provisions that require a company to commence insolvency proceedings. Canada does not have legislation that imposes liability on directors when a company carries on business while it is insolvent or nearing a state of insolvency. As a general rule, unless the insolvent business is carried on in a manner intended to defeat or delay the claims of creditors or deliberately perpetrate harm or financial loss, there are no specific legislative remedies available apart from the 'oppression remedy' - a remedy arising under corporate legislation. The oppression remedy is a broad equitable remedy which permits the court to review and order appropriate rectifying relief in favour of creditors where a corporation or its directors have acted in a way that is oppressive or unfairly prejudicial or that unfairly disregards the interests of the creditors affected. This is an exceptionally broad power and is frequently invoked by creditors who have been harmed by the actions of a corporate debtor. The creditor will be required to prove that the impugned conduct was the legal cause of the harm alleged to have been suffered by the creditor.

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

During both BIA and CCAA reorganisations, the debtor typically continues to carry on business in the normal course. BIA proposal trustees and CCAA monitors must be appointed in reorganisations, but they do not normally play an active role in the debtor's business operations during a restructuring except for transactions that are outside the ordinary course of business. Significant transactions that are out

of the ordinary course of the debtor's business must be submitted to the court for its approval. The role of trustees and monitors is generally confined to monitoring and reporting to the creditors and to the court as to the debtor's business and operations, and the debtor's progress in its reorganisation. During a reorganisation, parties to contracts with the debtor are prohibited from terminating their agreements on the grounds of insolvency, but they may require that the debtor pay for goods and services in cash. A new provision in the CCAA effective in September 2009 allows the court to compel a critical supplier to continue to supply to a debtor on the security of a charge against the debtor's property for the value of the goods or services supplied.

In reorganisation proceedings, directors and officers can usually (subject to an order to the contrary by the supervising court) carry on business in the ordinary course in normal and routine matters that do not require the approval of the court. In liquidations, where a licensed insolvency trustee is appointed, the assets and business of the debtor company vest in the trustee and the directors and officers have no further authority to act on behalf of the company. The result is the same in the case of receiverships, although the assets of a debtor corporation do not vest in a receiver in a receivership proceeding. In appropriate cases, the receiver may elect to operate the business in order to generate value and sell the business as a going concern.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

In a BIA reorganisation, an automatic stay of proceedings is imposed on secured and unsecured creditors. However, the stay does not apply to those secured creditors who took possession of their collateral before the filing or who gave formal notice of their intention to enforce their security more than 10 days before the filing. The court can lift a stay in a BIA reorganisation if the creditor is likely to be 'materially prejudiced' by the stay or if it is otherwise equitable that the stay be lifted.

In a BIA liquidation, there is an automatic stay of proceedings by unsecured creditors, but the stay does not affect secured creditors who are generally free to enforce their security outside of the liquidation process. A limited stay of a secured creditor's realisation in a liquidation can be sought from the court by the trustee to preserve the value of the assets of the estate. Although an unsecured creditor can apply to the court for relief from the stay, unsecured creditors are virtually never permitted to pursue seizure remedies.

In a CCAA reorganisation, a very broad stay of proceedings is imposed against both secured and unsecured creditors. The initial period of the stay is limited to 30 days, although the stay period is usually extended by the court if the debtor is working constructively toward a suitable plan of arrangement. The CCAA contains no specific provisions dealing with relief from the stay but, in general, stays have been lifted where a debtor's plan was likely to fail or where the debtor showed no progress in developing a plan of arrangement.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Until September 2009, there was no specific provision in either the BIA or the CCAA for post-filing priority secured credit, although some courts had allowed priority liens over existing security in cases of urgency. New provisions under both Acts now allow funding analogous to US debtor-in-possession financing. The new provisions allow the court to grant charges over the debtor's assets having priority over existing security. Under Canadian practice, there are fewer protective provisions regarding post-filing secured credit. For example, there is no provision for 'adequate protection'. A reorganising company with a viable prospective restructuring, however, will be permitted to borrow and grant security ranking ahead of the claims of unsecured creditors.

There is no 'administrative expense priority' available under either the BIA or CCAA for general post-filing credit obtained by the debtor in the normal course. While both Acts contain provisions that creditors are not obliged to supply on credit, the CCAA also allows a court to

order that a critical supplier continue to supply, on the basis of security over the debtor's property.

### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Canadian law recognises claims for 'legal set-off' and 'equitable set-off' in liquidations and reorganisations. Legal set-off requires that claims be both liquidated and mutual. Equitable set-off can exist regardless of whether debts are liquidated. Instead, the court looks at the connection between the various claims in respect of which set-off is asserted. If the connection between such claims would make it unfair or inequitable to permit one party to recover its claim without permitting the other party to set off what is owed to it, the courts will permit the claims to be set off against each other.

Valid set-off claims are expressly preserved in the BIA. In a CCAA reorganisation, the initial court order may temporarily restrain the exercise of rights of set-off. Set-off will, however, be recognised and permitted for the purposes of creditors' claims in a CCAA plan. Both the BIA and CCAA contain special provisions that expressly permit netting of particular types of financial contracts such as swaps, repurchase agreements and commodity contracts.

### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

In liquidations under the BIA, the assets of the debtor (apart from assets that are subject to secured claims and assets that are held in trust) vest in the licensed insolvency trustee who is empowered to sell them with the permission of the inspectors of the estate. Sales of assets out of the ordinary course of business and, particularly, a sale of the debtor's business as a whole, require the permission of the court.

The rights of the debtor in a CCAA reorganisation to sell assets are set out in the court order that grants protection to the debtor. Sales of assets in the ordinary course of business are permitted, but sales out of the ordinary course of business, including a sale of the debtor's entire business, requires the permission of the court.

In both BIA and CCAA proceedings, it is possible to conclude a sale of assets of the debtor, including a sale of substantially all of the assets of the debtor, without the necessity of awaiting a formal BIA Proposal or CCAA Plan. However, the court may not approve a sale unless it is satisfied that the debtor 'can and will' make the employee and pension plan payments required for approval of a BIA proposal or a CCAA plan.

Stalking horse bids are becoming more common, but are not yet routine in Canadian proceedings. In such cases, it must be demonstrated that the sale transaction is warranted, the sale will benefit the stakeholders, no creditor objects to the sale and there are no better alternatives. If approved by the court, a publicised sale process is conducted in which superior bids are sought before a bid deadline, with a possible auction in the event there are multiple bids. Competing bids generated through this process will have to exceed the original bid price plus the break fee (representing the original bidder's participation costs) in order to be considered a superior overbid.

There has recently been limited acceptance of credit bidding in asset sales – in other words, allowing a secured creditor to bid some or all of its debt in lieu of making payment in order to acquire the assets to which its security attaches. Subject to the discretion of the court, secured creditors can bid up to the full face value of the secured claim, even if the value of the claim exceeds the fair market value of the assets. In considering a stalking horse credit bid, a court will require that the sale process allow sufficient opportunity for superior bids to be submitted. Where the debtor is particularly distressed, a court may consider a 'pre-pack' or 'quick flip' sale under the BIA or CCAA provided the court

has evidence that there has been some form of reasonable marketing process, the sale maximises recovery and is supported by creditors. Support of the proposed monitor or court-appointed receiver will also be crucial.

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

The commencement of bankruptcy proceedings under the BIA does not automatically terminate a contract. A bankruptcy trustee is entitled to step into the shoes of the debtor and perform a contract (except for those that are personal in nature, such as employment contracts), and to require the other party to perform it as well. If, however, the trustee does not begin fulfilling the debtor's obligations under a contract within a reasonable period, the other party can treat the contract as terminated.

A bankruptcy trustee of a licensee may disclaim an agreement with the licensor. Although new provisions allow for a restructuring debtor to disclaim agreements, an agreement for the use of intellectual property rights may not be disclaimed by the restructuring debtor or the trustee of a licensor as long as the counterparty continues to perform its obligations under the agreement.

Under the CCAA, a debtor remains in possession of its property and therefore continues to have the benefit of contracts to which it is a party. A CCAA initial order will typically prohibit third parties from terminating their agreements with the debtor.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

Although the BIA and CCAA are silent in respect to the use personal information and privacy, the collection and use of personal information by private Canadian companies in the course of commercial activities in Canada is governed federally by the Personal Information Protection and Electronic Documents Act (PIPEDA) or by equivalent provincial legislation. Under this legislation, a business is required to obtain consent to collect, use and transfer an individual's personal information.

'Personal information' is broadly interpreted, meaning that privacy legislation will impact the manner in which a debtor, licensed insolvency trustee or court-appointed receiver use or transfer personal information in insolvency matters. As determining whether consent was properly obtained may prove to be difficult or create an impediment to realisation efforts, parties often seek a court order that limits the need to obtain express consent in appropriate circumstances – such as in the context of a court-approved sale process. To that end, template court orders have been developed across Canada for use in insolvency proceedings that allow for personal information to be disclosed to prospective purchasers under confidentiality orders. In some cases, such as with personal health information, the purchaser may be required to notify the individual of the transfer and provide an opportunity to transfer such information if requested.

Related to the use and disposition of personal information is the ability to communicate with third parties, for instance, as part of a sale process. Canada's Anti-Spam Legislation (CASL) prohibits the transmission of a 'commercial electronic message' unless prior consent has been obtained from the recipient or the communication falls within one of the statutory exemptions. As the distribution of court orders, notices and other correspondence to stakeholders or interested parties in insolvency proceedings may be precluded under CASL, a court may grant an order exempting the application of this legislation on the basis that it would enhance a restructuring or realisation efforts, or both, for the general benefit of stakeholders.

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### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

In both CCAA and BIA reorganisations, a restructuring debtor may disclaim burdensome or unfavourable contracts with the approval of the monitor or trustee or the court. Disclaimers are carried out by a simple notice or letter delivered to the counterparty. Counterparties who wish to challenge the disclaimer must apply to court for relief within 15 days of receipt of the disclaimer. In determining whether to uphold a disclaimer, the court will consider, *inter alia*, the prospects for a viable restructuring and whether the disclaimer will create significant financial hardship for the counterparty. Counterparties whose contracts have been terminated may file an unsecured claim in a CCAA debtor's plan or a BIA debtor's reorganisation proceedings for the damages caused by the termination. Certain types of contract, however, cannot be disclaimed, such as collective bargaining agreements, financing agreements where the debtor is the borrower, and leases of real property if the debtor is the lessor.

Where a breach of contract occurs after an insolvency case is opened, the other party must be careful not to contravene the statutory and court-ordered protections that are given to the debtor. In most cases, this will require the other party to the contract to obtain the approval of the court for the exercise of any remedies against the debtor or even, if the court order prohibits it, for permission to cease its performance under the contract. This type of approval is rarely granted in *bona fide* reorganisations.

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### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

There are no specific provisions in the BIA or CCAA relating to arbitration processes. To the extent that arbitration proceedings are in progress at the time of the debtor's filing, they would be subject to any applicable stay of proceedings.

Within insolvency proceedings, there is judicial precedent for referring stakeholder disputes to alternative forms of dispute resolution such as mediation. Moreover, the practice in CCAA cases is to delegate responsibility for resolving creditor claims to 'claims officers', who are often senior insolvency lawyers or retired judges. Decisions of claims officers are subject to a right of appeal to the court.

There are no specific provisions that preclude particular types of disputes from being arbitrated. In general terms, disputes that involve the application of public laws or policies that are regarded as matters of public policy or public order are considered to be non-arbitrable. Disputes in insolvency cases can be arbitrated, but the permission of the supervising court should be obtained in advance so as not to contravene any applicable court order and not to conflict with any procedures under way before the court.

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### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

There are few statutory requirements for a debtor's BIA proposal or CCAA plan. A BIA proposal must, however, provide for the prompt payment of certain preferred claims, including employee wage claims and certain governmental claims.

Both CCAA plans and BIA proposals must be accepted by a 'double majority' of creditors (ie, by 50 per cent in number holding two-thirds in value of the unsecured creditors voting on a BIA proposal and by 50 per cent in number holding two-thirds in value of each class of

creditors voting on a CCAA plan) and approved by the court. Creditor classes in CCAA proceedings are established based on a 'commonality of interest' test. The court will approve a plan or proposal that has been accepted by creditors as long as it is 'fair and reasonable' from the point of view of the general body of creditors.

A BIA proposal or plan of reorganisation may provide releases for non-debtor third parties provided that it is demonstrated that the releases are rationally related to the purpose of the plan or proposal, that they are essential to the success of the plan, that they are not overly broad or offensive to public policy and that the parties receiving the releases contributed to the successful plan or proposal.

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### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

Neither the BIA nor the CCAA contains formal procedures for implementing expedited reorganisations. Nonetheless, the provisions of both statutes are flexible enough to accommodate pre-packaged reorganisations at a very early stage in restructuring proceedings. With sufficient advance planning and creditor consultation and support, 'pre-packaged reorganisations' can be accommodated in both BIA proposals and CCAA plans.

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### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A BIA proposal must be approved by at least 50 per cent in number and two-thirds in value of the claims of unsecured creditors voting on the proposal. If this approval is not received from the creditors, the debtor is automatically placed in liquidation. If a secured creditor class votes against the proposal, an automatic liquidation does not take place, but the stay of proceedings against the secured creditors of that particular class ends. A proposal will also fail if the court refuses to approve it. Subsequently, if the debtor defaults in performing a proposal that has been approved by creditors and the court, the court may annul the proposal, which leads to an immediate liquidation of the debtor's assets, although transactions properly undertaken during the reorganisation period are not nullified.

Under the CCAA, there is no automatic liquidation if unsecured creditors reject the CCAA plan, but the court-imposed stay of proceedings is usually terminated and creditors may exercise their remedies. This could include a request to place the debtor into liquidation proceedings under the BIA. A secured creditor class that votes against the plan may thereafter deal with its security regardless of whether the plan succeeds or fails. Failing to obtain support from major secured creditors may jeopardise the liability of a plan. As in the BIA, the court must approve a plan before it becomes effective.

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### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

In a BIA liquidation, the bankruptcy trustee is required to call a meeting of creditors within 21 days of the commencement of the bankruptcy, by written notice to all creditors providing specified information regarding the administration of the estate, and the assets and liabilities of the debtor, in a formal report from the trustee. The trustee is required to report on the financial condition of the estate to all of the creditors if directed to do so by the inspectors of the estate or to an individual creditor when requested to do so by the creditor. The books and records of the estate are available to be inspected by the inspectors or the creditors or their representatives. There are no comparable provisions in the CCAA. Where a court-appointed receiver has been appointed, the receiver is required to immediately deliver a statement to all stakeholders listing the assets and liabilities of the debtor. The receiver will also provide periodic reports to the court and all stakeholders.

Meetings of creditors must also be called in BIA reorganisation proceedings for the creditors to vote on the debtor's proposal. Subsequent meetings are not mandatory and are generally rare. The only statutory committee of a BIA estate is the board of inspectors, which is elected by the creditors at the first meeting of creditors. In general, the inspectors review and verify the operation and finances of the estate as well as review and consider the trustee's administration. Creditors may form unofficial committees, but such committees need not be recognised by the trustee or the court and are not funded by the estate. Reorganisational proceedings under the BIA do not specifically require the appointment of inspectors, although their appointment is common in BIA reorganisations. Creditors are able to initiate proceedings to pursue remedies against third parties or seek changes in the administration of the estate. As discussed above in question 23, a BIA proposal or plan of reorganisation may provide releases in favour of non-debtor third parties.

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### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

If the bankruptcy trustee under the BIA fails or is unable to pursue remedies that would benefit the estate, a creditor may, with court approval, pursue the remedies and any benefit received will belong to that creditor and other participating creditors to the extent of their claims and applicable costs. Any surplus must be paid to the bankruptcy trustee. The distinctive feature is that creditors who do not participate in the proceedings do not share in any of the recoveries unless there is a surplus paid to the estate.

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### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The court has a wide discretion to appoint legal and financial representatives on behalf of creditor groups in CCAA or BIA reorganisations. Such appointments are typically made in larger and more complex CCAA proceedings so as to provide representation for particular stakeholders, such as current and retired employees who may otherwise lack resources to participate effectively in the restructuring. Creditor representatives are appointed on application made on notice to affected secured creditors. Their powers and responsibilities are defined in the appointment order. Funding for their professional charges is normally secured by a court-ordered priority charge on the assets of the reorganising debtor. There is a form of creditors' committee in BIA proceedings, but its primary function is to provide advice to the trustee and it does not have separate legal representation in the proceedings. There are no formal committees in CCAA cases although informal committees (which are self-funded) are usually recognised in CCAA cases.

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### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Neither the BIA nor the CCAA specifically contemplates the procedural or substantive consolidation of debtor corporations. However, it is common for multiple insolvent affiliated corporations to make simultaneous filings under the CCAA or the BIA. These proceedings are often heard by the court at the same time for procedural efficiency, although corporate distinctions between the group members are still maintained.

There have been some cases in which affiliated corporations have reorganised their affairs on a consolidated basis under the CCAA but, where this has occurred, it has usually been on a consensual basis. Canadian case law on the consolidation of affiliated corporations is very limited.

The transfer of assets to an administration outside of Canada is relatively rare, but there is nothing in principle that would prevent such transfers in aid of a restructuring provided that court-approved safeguards for affected stakeholders are first put in place.

## Appeals

### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

The pathway for an appeal of a court order made in an insolvency proceeding is dictated by the legislation governing the proceeding. In the case of a proceeding instituted under the BIA, an appeal is governed by both the BIA and provincial rules of court. If the court order involves future rights, it is likely to affect other cases of a similar nature in bankruptcy proceedings, involves property exceeding \$10,000 in value or relates to the granting of or a refusal to grant a bankruptcy discharge, the appellant has an automatic right of appeal to a provincial appellate court. Where the issues in the appeal do not fall within these categories, one will need to seek leave (permission of the court) in order to proceed with an appeal. The factors to be considered on an application for leave to appeal are: whether the issues in the proposed appeal are of significance to the practice in bankruptcy/insolvency matters; whether the appeal is meritorious and; whether the appeal will unduly hinder the progress of the bankruptcy/insolvency proceedings.

By contrast, appeals are not allowed as a right from orders made in CCAA proceedings. Leave to appeal from orders under the CCAA are granted sparingly and only where there are serious and arguable grounds that are of real and significant interest to the parties. The rationale for restricting appeals is that the CCAA seeks to resolve matters and obtain finality on the debtor's restructuring efforts without undue delay. The factors considered by a court on such applications include:

- whether the point in the appeal is of significance to insolvency law generally;
- the point raised is of significance to the action itself;
- whether the appeal is, at first impression, meritorious or frivolous; and
- whether the appeal will unduly hinder the progress of the action, including a consideration of the prejudice to the parties.

There is no requirement to post security under either the BIA or CCAA. However, security may be required to be posted under provincial rules of court. A responding party to the appeal may also seek an order compelling the party bringing the appeal to post security with the court in appropriate circumstances.

Where an appeal has been brought under the BIA, the order appealed from is stayed until the appeal is disposed of unless an appellate court cancels or varies the stay. Under the CCAA, the appellant must apply for an order staying the order under appeal. In such cases, it must be established that the stay would be in the interests of justice.

## Claims

### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Both secured and unsecured creditors must file proofs of claim with the BIA trustee or CCAA monitor, including creditors with contingent or unliquidated claims. In the BIA, there is no statutory time limit for filing proofs of claim, but a creditor that does not file a proof of claim cannot vote at meetings of creditors and will not receive a distribution on its claim. Once a proof of claim has been filed, the trustee or monitor either accepts or disallows the claim. A creditor that is dissatisfied with a decision of the trustee or monitor may appeal the decision to the court.

Bar-date procedures for filing claims in a CCAA reorganisation are usually created by a separate court order and are not provided for in the

statute. The court order will also prescribe the procedure for the creditor to follow on a disallowance of its claim by the monitor.

Neither the BIA nor the CCAA contain provisions dealing with the purchase, sale or transfer of claims against the debtor. A transferee of a claim must provide formal notice of the transfer to the trustee or monitor to confirm the transfer.

Claims are determined in a summary manner by the BIA trustee or the CCAA monitor, subject to appeals to a court-appointed claims officer or the court or both.

If a proper and valid claim is acquired at a discount, it can be enforced for its full face value, absent any improper conduct by the holder of the claim. Interest on unsecured claims, with rare exceptions (as in a plan that provides for post-filing interest), will cease to accrue on the opening of a case and interest will not be payable thereafter on unsecured claims unless there is a surplus remaining after the payment of the principal amount of all claims. Interest on secured claims continues to accrue after the opening of a case up to the value of the collateral subject to the security interest.

## Modifying creditors' rights

### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

Canadian experience in this area is limited, but continues to develop. In a handful of cases, it has been suggested that a court may modify the priority of creditors' claims under the BIA to remedy unfair conduct. Other statutory measures exist to modify priorities in cases involving improper conduct.

## Priority claims

### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Excepting employee-related claims, major priority claims in liquidations and reorganisations include governmental claims for taxes withheld from employees' wages, environmental clean-up costs, and real property taxes. Property held in trust by the debtor is not included in the property of the estate. Ranking below secured creditors under the BIA are specified preferred claims, such as administrative expenses, certain municipal taxes and rent arrears. Under the CCAA, there are no statutorily specified preferred creditors, although CCAA orders often provide for comparable priority claims. After secured and preferred creditors have been paid in full, unsecured creditors receive any remainder on a pro rata basis.

## Employment-related liabilities in restructurings

### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

The two common types of employee claims that arise when employees are terminated in restructurings or liquidations are for 'termination pay' and 'severance pay'. Under Canada law, an employer must provide 'reasonable notice' when an employee's employment is terminated. As such, when employees are terminated without such notice they are entitled to termination pay for the notice period to which they were entitled, which usually depends on the length of their employment with the employer. In addition, special rules for termination pay may apply where the employment of 50 or more employees is terminated within a short and specific period of time (eg, four weeks). These special rules vary from province to province in Canada. Claims for termination pay generally rank as unsecured claims in restructurings or liquidations. Some provinces additionally provide for severance pay according to a legislatively prescribed schedule which depends on the employees' seniority and the length of employment with the employer. Severance pay claims also rank as unsecured claims in restructurings and liquidations.

Employees are also given priority claims ranking ahead of all creditors for unpaid wages over the debtor's liquid assets (ie, inventory, cash and accounts receivable) where the debtor is bankrupt or the subject of a receivership. This priority usually results in claims for unpaid wages being paid in full. A similar priority is given to employees for arrears

of contributions to employee pension plans. There has been recent litigation in Ontario over the priority of pension plan deficiency claims, which is discussed further in question 35.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Provincial governments in Canada generally regulate pension obligations and set procedures to determine the extent of employers' obligations under pension plans. Pension plan deficiencies in defined benefit pension plans are generally treated as unsecured claims against an employer in insolvency proceedings. Where a pension plan is being wound up prior to insolvency proceedings being commenced, however, the pension plan deficiency will be given a super priority status with priority over the claims of other creditors including secured creditors. Such contributions are generally treated in this way regardless of whether the employer is undergoing a bankruptcy proceeding.

In formal bankruptcy proceedings, the priority of pension deficiency claims is determined by federal insolvency legislation under which deficiency claims are generally treated as unsecured claims against the insolvent employer. However, unremitted amounts deducted from employee's salaries and amounts required to be paid by the employer to the pension fund are the subject of a super-priority claim. There has recently been significant litigation over pension plan deficiencies in insolvencies in Canada in which the courts have considered such non-insolvency issues as the extent of the duties of the employer to the pension beneficiaries on the particular facts involved.

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remedying the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Canadian environmental legislation imposes duties and remediation responsibilities on anyone who has had management or control over property having environmental problems. These duties and responsibilities (including remediation responsibilities) extend to directors and officers of corporations that have environmental problems, even if they are no longer involved with the corporation. Moreover, to avoid liability, directors and officers must affirmatively prove that they acted properly and prudently to avoid environmental problems which can be a difficult onus to discharge. In insolvencies, the environmental authorities are given a super-priority first charge for the costs of remediation over the affected property. In addition, insolvency administrators are given special protection from environmental liabilities created by the debtors.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

In a BIA liquidation, debtors are not released from pre-filing liabilities arising from fraud or from fines and penalties imposed by a court. In both BIA and CCAA reorganisations, the debtor and any purchaser of the debtor's business are bound by collective bargaining agreements (labour agreements with unions) and remain liable for environmental clean-up costs. Further, pre-filing secured creditors continue to have claims against pre-filing and post-filing assets of the debtor in which they have been granted a security interest. Contractual claims against directors cannot be compromised under a BIA proposal or a plan of reorganisation.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In a BIA liquidation, the trustee must first make payment of priority claims before making distributions to unsecured creditors. In a major case, a trustee will often make one or more interim distributions to

unsecured creditors. A final distribution is made to unsecured creditors once all of the property of the debtor has been realised and all claims against the estate have been settled.

Under a BIA proposal or a CCAA plan of reorganisation, distributions are made in accordance with the terms of the respective proposal or plan. Since plans and proposals are tailored to the specific debtor, distributions times and amounts will vary.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The BIA, in both liquidations and reorganisations, allows the bankruptcy or proposal trustee to apply to the court to annul certain transactions. The CCAA allows the monitor to use the BIA provisions. The transactions that are subject to challenge, include:

- transactions at an undervalue (TUVs), namely, transactions in which the consideration received by the debtor is less than the fair market value given by the debtor;
- preferences that, in the case of arm's-length creditors, are transactions made with the intent to prefer the creditor within three months of the date of bankruptcy or, in the case of non-arm's length creditors, transactions within 12 months of bankruptcy that have the effect of giving a preference to the creditor; or
- dividends that are paid when a corporate debtor is insolvent.

For TUVs, the court may annul the transaction or order that any party to the transaction (or any person privy to the transaction) pay the difference between the consideration and the fair market value involved in it.

Trustees may also use provincial avoidance legislation to challenge pre-bankruptcy transactions. If a transaction is annulled, the trustee may recover property from the purchaser, unless the purchaser is a bona fide purchaser for value.

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

Canadian law does not use the concept of a 'suspect period'. Time limits in which pre-bankruptcy transactions can be attacked are prescribed by the BIA. In bankruptcies, voidable transactions can be challenged only by the trustee in bankruptcy or by creditors to whom the trustee has assigned the remedy.

Transactions can be attacked in a BIA proposal in the same manner as in a BIA liquidation. The CCAA now incorporates the BIA's avoidance provisions.

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### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Directors are liable to employees for up to six months' arrears of wages for services performed by the employees during their directorships. Additionally, directors are liable for certain amounts payable by the corporation to governmental revenue authorities, such as unremitted source deductions (eg, income tax, government pension plan contributions, employment insurance premiums deducted from employees wages and, in certain circumstances, sales (VAT) taxes that were collected but not paid by the corporation prior to bankruptcy). Directors may escape liability for these payments if they exercise the 'due diligence' and skill of a competent director.

Officers and directors can also, in general, be found to be personally liable for offences committed by the corporation if the officer or director directed, authorised or participated in the commission of the offence. Directors and officers have a general corporate duty to act honestly and in good faith and have fiduciary duties to the corporation.

### Update and trends

The most controversial current issues in insolvency in Canada involve liabilities and priorities involving pension deficiencies, provincial builders' liens and responsibilities and liabilities in connection with environmental problems in the private international law context. The Supreme Court of Canada has recently clarified that judgment creditors wishing to enforce a foreign judgment in Canada do not need to establish a real and substantial connection to the Canadian court, potentially facilitating the ability to enforce a foreign judgment. Canadian law and practice in these major areas is continuing to evolve.

Directors and officers have been held not to owe fiduciary duties to creditors when the company is insolvent. The court has discretion to remove a director if it is demonstrated that the director is 'unreasonably impairing' the possibility of a viable restructuring, or is otherwise not acting in the best interests of the debtor. The court may fill any vacancy created by reason of a removal.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Canada has some limited examples of corporate control group liability legislation that is intended to create parent or affiliate corporation liability for the debts of subsidiaries and affiliates. Federal and provincial legislation does, however, provide courts with a broad equitable jurisdiction to hold corporations or their affiliates liable to stakeholders where corporate actions are determined to be oppressive or unfairly prejudicial to the interests of stakeholders (see also the discussion on substantive consolidation in question 29).

In the recent historic decision arising from the global insolvency of Nortel Networks, both the US and the Canadian courts ordered that the sale proceeds arising from the sale of Nortel's lines of business and intellectual property be allocated pro rata among the various international Nortel subsidiaries based on the percentage of allowable claims against each Nortel entity to the total allowable claims to all Nortel entities. The courts made it clear that this allocation mechanism did not constitute a global substantive consolidation as each entity remained separate and the funds allocated to each entity would be separately administered. Although the Canadian appellate court refused to grant leave to appeal the trial decision, the outcome of the US appeal has not yet been determined.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Insiders and non-arm's length creditors may generally assert legitimate claims in the bankruptcy of their corporations. Equity claims are statutorily subordinated such that non-equity claims must be paid in full before equity claims (ie, claims relating to ownership of shares or stock in a company) are paid. In BIA restructurings, a creditor who is related to the debtor may vote against but not for the acceptance of a plan of reorganisation.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Liquidations can be carried out in receiverships, which is a creditor's remedy against the debtor's business. Although receivership is also available as a court-ordered remedy, receivership can be an out-of-court procedure where a secured creditor appoints a receiver under its security to take possession of all or part of the debtor's assets that are subject to its security. The receiver will usually sell the debtor's business. Liquidations of businesses in out-of-court receiverships are becoming less common in Canadian practice, but are still often encountered in smaller cases.

Secured creditors with security on moveable property can enforce their security by seizure and sale either in court or out of court. Creditors with security on immoveable property can take possession of and retain the property in satisfaction of their claims through court proceedings or sell the property out of court or in court proceedings to satisfy the obligations owed to them.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Under new amendments to the BIA and the CCAA, the court may order the amendment of the debtor's constating documents (ie, its articles of incorporation, by-laws and shareholder agreements) to reflect the terms of the debtor's plan or proposal and can dispense with the requirement of shareholder approval. The CBCA and comparable provincial legislation allow shareholders to carry out non-insolvent liquidations and also provide for liquidation under the supervision of the court. A court liquidation may be instituted by the corporation itself (voluntary cases) or by a shareholder or creditor (involuntary cases).

The 'arrangement' procedures in the CBCA and comparable provincial legislation that allow exchanges of securities and amalgamations have been used increasingly in complex reorganisations either separately or in conjunction with insolvency procedures.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

A corporate debtor in liquidation under the BIA can only obtain a discharge from bankruptcy by paying all of its creditors in full, which is usually accomplished by means of a BIA proposal. A liquidation case can conclude once the trustee has distributed the assets to the creditors and has obtained its discharge from the court upon reporting on the administration of the estate.

A reorganisation in a BIA proposal is completed when the proposal is fully performed and a certificate of completion is issued by the proposal trustee. A CCAA reorganisation concludes when the CCAA plan is fully performed and the monitor is discharged by the court.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

In the latest amendments to the BIA and the CCAA, Canada adopted a 'concurrent proceedings' model that encourages cooperation by Canadian courts with courts in other jurisdictions. Canadian courts are empowered to make orders and grant relief to facilitate or implement arrangements that will coordinate Canadian proceedings with foreign proceedings. There is no distinction between domestic and foreign creditors as to their ability to commence insolvency proceedings, prove claims and share in the proceeds of the estate. Foreign judgments between parties tend to be recognised in Canada if the foreign jurisdiction had 'substantial contacts' with the parties and the matters at issue in the proceedings and provided that the enforcement of the judgment does not contravene Canadian public policy. A Canadian court order is required to enforce a foreign judgment. A foreign corporate liquidation is entitled to recognition if it is made in the corporation's country of incorporation. Canada is not a party to any bilateral or multilateral insolvency convention.

Canada has adopted some provisions of the UNCITRAL Model Law. The Canadian provisions relating to the Model Law, however, differ from most other adaptations of the Model Law in that the text of many of the articles has been changed and over 30 per cent of the articles in the Model Law have been partially or entirely omitted from the Canadian version. For example, provisions relating to access by foreign

representatives to domestic Canadian proceedings, notification to foreign creditors, and provisions for relief pending the determination of an application for recognition of a foreign proceeding are not present in the Canadian provisions. Nevertheless, it is expected that Canadian courts will continue in their long-established tradition of cooperating with foreign administrations.

#### COMI

**48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

The general approach of Canadian courts is to determine the location of the registered (head) office of a corporate debtor. The COMI of the debtor will then be presumed to be in that jurisdiction. This presumption can be rebutted by evidence showing that the head office functions of the debtor are located in another jurisdiction. The test is to establish where the 'nerve centre' of the debtor's business is located and that jurisdiction will be regarded as its COMI for insolvency purposes. Thus, in several cases, the COMI of a company incorporated in Canada and with its head office in Canada has been held to be outside Canada in the jurisdiction of the parent company where the debtor was a member of a corporate group that was operated and controlled in the other country. Canadian courts have identified three main criteria for determining the location of the COMI of a debtor: the location is readily ascertainable by creditors; the location is one in which the debtor's principal assets or operations are found; and the location is where the management of the debtor takes place. Reference in this regard can be made to the Principles for Coordination of Multinational Enterprise

Group Insolvencies that have been promulgated and approved by the membership of the International Insolvency Institute (at [www.iii-global.org](http://www.iii-global.org)).

#### Cross-border cooperation

**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

Canadian courts have long been receptive to cooperating with courts in other countries in multinational cases. Several Canadian courts have adopted and approved the use of the Guidelines for Court-to-Court Communications in Cross-Border Cases developed by the American Law Institute and the International Insolvency Institute. The objective in approving the Guidelines is to facilitate cooperative procedures in insolvency proceedings that involve cross-border and international cases. There are several recent examples of major cases (eg, *Nortel* and *AbitibiBowater*) where there has been careful coordination between Canadian courts and courts in other countries in the development and progress of cross-border reorganisations and restructurings, which has resulted in improved outcomes for stakeholders.

Canadian courts have a long history of recognising foreign proceedings and a strong history of cooperating with foreign courts in international insolvency proceedings and have rarely refused to recognise proper foreign proceedings or to cooperate and coordinate with foreign courts.



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**Cross-border insolvency protocols and joint court hearings**

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

Canadian courts have been receptive to recognising insolvency and reorganisational proceedings in other jurisdictions and to coordinating administrations of Canadian assets with administrations in other countries. The principal means of doing so is through the use of cross-border insolvency protocols.

Cross-border insolvency protocols have been adopted and approved by the courts in several dozen major cases involving Canada and the United States. Additionally, joint hearings have been held between courts in Canada and the United States in many recent cross-border reorganisations.

# Cayman Islands

Andrew Bolton and Andrew Jackson

Appleby

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Companies Law (2016 Revision) and the Companies Winding Up Rules 2008 (as amended) are applicable to corporate insolvencies. The Companies Law also provides a regime for what are known as arrangements and reconstructions, enabling companies to reach compromises or arrangements with their creditors or members, and a regime for the merger or consolidation of Cayman companies and Cayman companies with foreign companies.

It is noted that the corporate insolvency regime also applies to the winding up and dissolution of exempted limited partnerships and limited liability companies, save to the extent that it is varied by the Exempted Limited Partnership Law, 2014 and the Limited Liability Companies Law, 2016, respectively; and that the Bankruptcy Law (1997 Revision) applies to personal bankruptcies.

A debtor company will be insolvent if it is unable to pay its debts as they fall due for payment.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Insolvency proceedings will be commenced in the Financial Services Division of the Grand Court. Where an appeal from a decision of the Grand Court is possible, it would be made to the Cayman Islands Court of Appeal, and any possible appeal from the Court of Appeal would be made to the Judicial Committee of the Privy Council in England.

The court will have the power to wind up a company if:

- the company has passed a special resolution requiring it to be wound up by the court;
- the company does not commence business within a year of its incorporation, or suspends its business for a year;
- the period, if any, fixed for the company's duration by its articles of association expires, or an event occurs upon which the articles of association provide it is to be wound up;
- the company is insolvent; or
- the court is of the opinion that it is just and equitable that the company be wound up (eg, due to fraud, managerial misconduct, breakdowns of trust and confidence, loss of substratum).

The court thus has the power to wind up a company in each of the circumstances in which its winding up should be appropriate.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

All companies which are formed and registered under the Companies Law and the Limited Liability Companies Law, or which existed under Cayman Islands law prior to the original enactment of the Companies Law, may be susceptible to customary insolvency proceedings. A foreign company may also be susceptible to customary insolvency

proceedings, but only where it has property situated in the Cayman Islands, is carrying on business in the Cayman Islands, is the general partner of a Cayman Islands exempted limited partnership or is registered as a foreign company in the Cayman Islands.

Assets over which the company has granted a creditor security will be excluded from the insolvency estate. While the liquidator might realise such assets with the consent of the secured creditor, the net proceeds after deduction of the liquidator's costs can be paid only to the secured creditor.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There are a number of entities that the government has established to perform particular public functions. Such entities are created by specific enactments which generally do not address what is to happen in the event of their insolvency. The government generally provides subsidies, as needed, to ensure insolvency does not occur.

In the event that the government decides that a particular entity should be dissolved, it will typically need to enact specific legislation to achieve that purpose, for example, the Health Services Authority (Dissolution) Law 1993, which dissolved the Health Services Authority and vested all of its property, rights and liabilities in the government. One exception is the Cayman Islands Development Bank, in respect of which the Monetary Authority is given specific powers under the legislation that established the bank to (among other things) appoint a person to advise the bank on the proper conduct of its affairs where the bank is or appears likely to become insolvent and to report to the Monetary Authority thereon within three months of his appointment; upon receipt of the report, the Monetary Authority will have power to (among other things) permit a reorganisation of the bank's affairs or request that it be wound up.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No such legislation has been enacted.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

The principal type of security which is taken on immovable property in the Cayman Islands is a registered charge, all land in the Cayman Islands being registered. The charge will not transfer title to the immovable property to the chargee, but will entitle the chargee to take steps in the event of non-payment, typically leading to a sale of the charged property.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

The principal types of security which are taken on moveable property are mortgages, fixed and floating charges, liens and pledges.

A mortgage will involve a transfer by the mortgagor of its interest in the mortgaged property to the mortgagee to secure repayment, subject to the mortgagee's right to redeem its interest in the property upon repayment.

A fixed charge is a security interest that the chargor grants over specific property (without transferring the specific property) to the chargee to secure repayment. It requires the chargor to retain the charged property and gives the chargee certain rights of enforcement against the charged property in the event of a default.

A floating charge is a security interest that the chargor grants over property it needs to remain able to deal with freely, but that will crystallise into a fixed charge over the property it holds, and give the chargee rights of enforcement against such property in the event of a default in repayment.

A lien may arise by operation of law where a creditor has lawful possession of an asset and payment is due to him for services rendered to the owner. The creditor may retain the asset until payment is made, but will not be entitled to sell it to settle the account.

A pledge will involve a debtor depositing goods with his creditor to secure his debt, which the creditor may then sell if the debtor fails to meet its obligation to pay the debt.

Contracts for the sale of goods may also provide for the supplier to retain title to the goods until full payment has been received, enabling it to call for the return of the goods in the event of default.

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## Unsecured credit

### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

An unsecured creditor will generally need to commence proceedings against a debtor company to recover its debt in the event of non-payment. If the debt is disputed, the proceedings are typically commenced by writ of summons. If the creditor obtains judgment in such proceedings for payment of the debt, it may then take steps to enforce its judgment against the assets of the company, and what step will be appropriate will depend on the nature of the assets against which enforcement is sought: for example, land and shares may be charged and, if necessary, sold; debts owed to the company may be garnished; and other moveable property may be seized by the Court's bailiff and sold. If the debt is not disputed, the creditor may prefer to serve a statutory demand for payment on the company and, in the event of non-payment, petition the court to wind the company up on the ground that it is insolvent. If the winding-up order is made, the creditor would then (at the appropriate time) prove its debt in the liquidation.

Proceedings commenced by writ can take between months or years to be decided, depending on how vigorously they are defended. Where there is no strong defence to a claim for payment, judgment may be delivered within a year or less. If the defence has no prospect of success, the creditor may even obtain summary judgment against the debtor and accelerate to the enforcement stage well within a year. The time it will take to enforce a judgment can also vary considerably depending on (among other things) the nature and location of the assets against which enforcement will be sought, and indeed whether those assets first need to be discovered.

The time it takes to carry out a liquidation will depend on the state of the debtor company when liquidators are appointed: if information is readily available and assets can easily be realised, the liquidation should be completed within a short time frame, but, if the opposite is found, the process could be very lengthy.

Pre-judgment attachments are not available under Cayman Islands law. A creditor may however apply to the court for an injunction restraining the debtor from disposing of its assets up to the value of the claim if (among other things) there is a real risk that the debtor will dispose of the assets to render a judgment against it nugatory or more difficult to enforce.

If a foreign creditor has obtained judgment in a foreign court against a debtor with assets situated in the Cayman Islands, it may seek to enforce that judgment against the assets in the Cayman Islands. Such enforcement will generally require proceedings to be commenced in the Cayman court claiming the judgment debt from the debtor (though there is a statutory regime that simplifies the enforcement of Australian judgments), and, once a Cayman judgment is obtained, it may then be enforced against the assets in the Cayman Islands by the usual processes.

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## Voluntary liquidations

### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A company may place itself into voluntary liquidation by a special resolution of its members, or its articles of association may require it to go into voluntary liquidation at a particular time or upon the occurrence of a particular event. Once the voluntary liquidation commences, the company will only be permitted to carry on business if and to the extent that doing so is beneficial for its winding up, and any share transfer will be void unless sanctioned by the liquidator. In order for the liquidation to continue as a voluntary liquidation (without the court supervising), the directors must swear a declaration of solvency within 28 days of its commencement. Provided the declaration is sworn, the person or persons appointed as voluntary liquidators will exercise their powers to wind up the company's affairs and distribute its assets, and the company will be dissolved thereafter.

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## Involuntary liquidations

### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

A creditor may place a debtor company into involuntary liquidation by petitioning the court on the ground that the company is insolvent and obtaining a winding-up order. Upon the making of the winding-up order, any disposition of the company's property and any transfer of shares or alteration in the status of its members made after the presentation of the petition will be void, unless the court otherwise orders. The winding-up order will also trigger the liquidators' obligations to collect, realise and distribute the company's assets to its creditors, and any surplus to its members, and to report to creditors and members on the liquidation.

As to the effects of the winding-up order on the commencement or continuation of legal proceedings against the debtor company, see question 14.

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## Voluntary reorganisations

### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

A debtor company may commence a formal financial reorganisation by petitioning the court for its approval of a scheme of arrangement. The scheme will be required to show some element of accommodation by both the company and its creditors or members (as the case may be), and will be required to provide sufficient information to enable creditors or members to reach an informed decision on the proposal. Procedurally, evidence will need to be filed describing the purpose and effect of the proposed scheme, and providing information that enables the court to determine whether meetings of classes of creditors or members should be convened and the appropriate composition of the classes. If creditor or member approval is obtained at properly convened meetings (see question 23), the court will be asked to approve the scheme, and may do so either absolutely or subject to certain conditions in light of any opposition to the scheme.

In conjunction with the scheme, the company may seek the appointment of provisional liquidators to trigger and take advantage of the statutory moratorium on claims. It is commonplace for provisional liquidators to be appointed for the purposes of proposing the scheme, as the law permits.

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**Involuntary reorganisations**


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**12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

The Companies Law does not permit a company to be reorganised involuntarily.

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**Mandatory commencement of insolvency proceedings**


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**13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

The Companies Law does not impose any obligation on a company to commence insolvency proceedings at any time. No civil or criminal liability will arise purely because a company in fact continued to trade after it had become insolvent. Criminal liability may, however, arise in such circumstances where steps have been taken by officers of the company (among others) with an intent to defraud its creditors. Additionally, any persons who were knowingly parties to the carrying on of the company's business with an intent to defraud its creditors or for any fraudulent purpose may be held liable to contribute to the company's assets. Directors may also incur civil liability where it can be shown that they breached their duties in permitting the company's business to be carried on while it was insolvent.

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**Doing business in reorganisations**


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**14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

There is no statutory restriction on a company carrying on business during the implementation of a scheme of arrangement, though the terms of the scheme may restrict or qualify the company's ability to do certain things (eg, obtaining credit). If provisional liquidators have been appointed in conjunction with the scheme, they may carry on the company's business for the purposes of the restructuring or, less frequently, may supervise the directors of the company in carrying on its business.

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**Stays of proceedings and moratoria**


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**15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

There is no prohibition against the continuation of legal proceedings or the enforcement of claims by creditors in a voluntary liquidation. However, once an order has been made for the winding up of a company under the court's supervision or for the appointment of a provisional liquidator, no legal proceedings (including arbitration proceedings) may be commenced or continued against that company without the permission of the court; the exception to this rule is that a secured creditor may enforce its security without first obtaining such permission. In determining whether to grant permission to commence or continue legal proceedings against the company, the court will consider whether it is right and fair to all parties to do so in the circumstances of the case, and whether it is necessary to impose any conditions on the granting of such permission to alleviate any potential unfairness. It is also noted that, in the period between the presentation of the petition and the making of a winding-up order, a creditor, member or the company itself may apply for an order staying any proceedings being pursued against the company before the local courts or restraining further proceedings from being pursued before a foreign court. While there is no reported local authority which indicates the matters the court will consider in determining whether to grant such an order, it is expected that the main consideration will again be what is fairest to all parties in the circumstances of the case.

There is no prohibition against the continuation of legal proceedings or the enforcement of claims by creditors in a reorganisation by way of a scheme or arrangement. However, the appointment of provisional liquidators may be sought in conjunction with the scheme to trigger and take advantage of the statutory moratorium on claims while the scheme is implemented.

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**Post-filing credit**


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**16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

There is no absolute legal prohibition against loans or credit being obtained by the liquidators of a company in liquidation or by a company undergoing a reorganisation: a liquidator may borrow and grant security over the company's assets with the court's permission, and a company's ability to borrow during a reorganisation by way of a scheme of arrangement will be delimited by the terms of the scheme.

Funds borrowed by a liquidator for the purposes of carrying out a liquidation will generally be expenses of the liquidation and would be paid in priority to the claims of preferred and other unsecured creditors in the liquidation.

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**Set-off and netting**


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**17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

Creditors remain able to exercise existing common law and contractual rights of set-off and netting as against a company following the commencement of its liquidation. In the case of an insolvent liquidation, save where the creditor had notice at the time the debt fell due for payment that liquidation proceedings had been commenced, set-off will be automatic, absent any contractual arrangement to disapply it. Where it applies, an account will be taken of what the company owes to the creditor and vice-versa as at the commencement of the liquidation and the balance after the set-off will be paid to the party to whom it is due.

In a reorganisation by way of a creditors' scheme of arrangement, the terms of the scheme may restrict or exclude rights of set-off or netting, if approved by the statutory majority of creditors and by the court.

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**Sale of assets**


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**18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

The terms of a scheme of arrangement may address matters concerning the sale of company assets or the company's entire business, if considered necessary. In a liquidation (save for a provisional liquidation for the purposes of reorganisation), the liquidator will be seeking to realise the assets of the company in the manner which produces the greatest return for creditors or members. The purchaser will acquire the assets on such terms as to liabilities and encumbrances as the sale agreement provides.

There is no prohibition on sales processes that involve 'stalking horse' bids or credit bidding. In a court-supervised liquidation, the court will, however, need to consider whether a sale on either of those bases should be approved as being likely to produce the best outcome for the creditors as a whole. While a sale agreement that permits 'stalking horse' bids may lead to the liquidator achieving a substantially better price for the asset, credit bidding is less likely to result in the best price being paid.

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**Intellectual property assets in insolvencies**

- 19** May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

The licence agreement will typically set out the circumstances in which termination of the licence by either party is permissible, or when termination will automatically occur. If the agreement does not provide for automatic termination in the event of insolvency, the company (and thus its liquidator) will continue to be entitled to make use of the rights until such time as the licence is terminated. The liquidator may terminate the agreement with the court's permission if appropriate, but would not be entitled to make use of the IP in any manner that is adverse to the interests of the licensor or owner.

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**Personal data in insolvencies**

- 20** Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

Where a company owes a common law duty of confidence to a person from whom it has received information, that duty will generally prevent the company from disclosing the relevant information. The Confidential Information Disclosure Law, 2016 (CIDL) lists a number of instances where the disclosure of such confidential information will not, however, constitute a breach of the duty of confidence and will not be actionable at the suit of any person: examples include disclosure in compliance with certain orders of the court and other authorities, in compliance with statutory obligations and to high-ranking police officers in connection with their investigation of a criminal offence; another key instance is where the person to whom the duty of confidence is owed consents to the proposed disclosure. If it were necessary for an insolvent company (acting by an officer or officers) to give evidence in its insolvency proceeding (which consisted of or included information it held in confidence for others and that it could not disclose under any such exception in the CIDL), it would be necessary for an application to be made to the court in a separate proceeding under the CIDL for directions as to whether the evidence should be given, and whether any safeguards should be imposed to maintain its confidentiality. If an insolvent company were contemplating transferring information that it held in confidence for others to a purchaser of all or part of its business, it would be prudent for it to seek the consent of the persons to whom the duty of confidence was owed before making such a transfer. The Cayman Islands presently does not have a statutory data protection regime, but draft legislation is presently under consideration.

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**Rejection and disclaimer of contracts in reorganisations**

- 21** Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

Cayman Islands law does not permit a debtor undergoing a reorganisation to reject or disclaim an unfavourable contract without the usual consequences for breach following. The debtor may nevertheless seek to renegotiate the terms of the contract if there is some prospect that the counterparty might agree to more favourable terms.

If there is a breach of contract by the company following the commencement of insolvency proceedings that gives rise to a claim for damages, the party having the claim will likely file a proof of debt in the liquidation. Where, however, the contract conferred a proprietary right on the counterparty prior to the commencement of the liquidation, the counterparty may call on the company for a transfer of the property and, if necessary, seek the court's permission to sue the company for the property.

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**Arbitration processes in insolvency cases**

- 22** How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Cases have arisen locally where a company has sought to restrain the presentation of a creditor's winding-up petition on the ground that the debt is disputed and the relevant agreement requires the dispute to be arbitrated. Recent judgments indicate that the court will require there to be a genuine and substantial dispute as to the debt before restraining the commencement of insolvency proceedings: if there is, the insolvency proceedings must be restrained in favour of arbitration.

The effect of the commencement of insolvency proceedings on the commencement and continuation of arbitration proceedings is addressed above in the response to question 15. An arbitration agreement between the company and a third party will remain enforceable after the commencement of insolvency proceedings and, where the liquidators wish to pursue a claim which the company has agreed to submit to arbitration, they may commence and continue the arbitration in respect of that claim with the permission of the court. If court proceedings were commenced in spite of an arbitration agreement, the defendant might assert its entitlement to have the dispute arbitrated and seek a stay of the court proceedings, but the court will not enforce that entitlement of its own motion.

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**Successful reorganisations**

- 23** What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

Mandatory features are addressed in the response to question 11. Creditors will be placed into classes for voting purposes if their legal rights are so dissimilar that they cannot sensibly consult with each other with a view to their common interest. The meeting or class meetings of creditors will need to be convened in accordance with directions from the court, and the scheme of arrangement will have creditor approval (but remain subject to court approval) where it is approved by a majority in number representing 75 per cent in value of those voting at the meeting or at each class meeting.

It is typical for a scheme to provide indemnities and releases to parties (particularly provisional liquidators) involved with its implementation. It is also possible that it may release non-debtor parties from liability, which might be appropriate where the benefit to the company in waiving its claim and retaining the party's services is considered greater than the value of the claim.

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**Expedited reorganisations**

- 24** Do procedures exist for expedited reorganisations?

There is no expedited scheme of arrangement process in the Cayman Islands. The speed with which a scheme of arrangement will obtain court approval will vary from case to case, and depends on (among other things) how quickly creditor or member approval can be obtained and the level and strength of any opposition to the scheme.

Members of a company may, however, choose to make use of the statutory merger and consolidation regime to effect a reorganisation, which is a streamlined out-of-court process requiring only members' approval of the proposed plan.

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**Unsuccessful reorganisations**

- 25** How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A reorganisation, either by scheme of arrangement or a merger or consolidation, will be defeated if it is not approved by the necessary majorities of creditors or members, as the case may be. A scheme of arrangement may also be defeated, even if approved by the requisite majorities, if the court refuses to approve it on the basis that it is

unfair or there is some sufficiently serious and justifiable objection to its implementation. In the case of a merger or consolidation, it will be open to a member of a constituent company to commence proceedings to challenge its validity on the ground that the statutory approval process was not complied with, or that it was approved on the basis of inadequate or incorrect information.

If a debtor company were to fail to perform a scheme, it is likely that a creditor would petition for its winding up and it would be placed into insolvent liquidation.

### Insolvency processes

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

Notice of the hearing of a creditor's winding-up petition must be advertised once in a newspaper circulated in the Cayman Islands and, where the company carries on business outside the Islands, once in a newspaper that is most likely to bring it to the attention of creditors there, unless the court directs that such advertisements are not required. Creditors will also be notified of (among other things) the making of a winding-up order and the appointment of official liquidators, as well as any meeting of creditors that is to be held and the liquidators' intention to declare and distribute a dividend.

In an insolvent liquidation, the liquidator will convene a first meeting of creditors primarily for the creditors to elect their liquidation committee. Thereafter, meetings of creditors may be held as often as the liquidator considers necessary, at creditors' requests, at the direction of the court and, in any event, not less than once per year. The liquidation committee will also meet on the dates or at the intervals that it resolves, as requested by any two of its members and, in any event, not less than semiannually.

Official liquidators will report to the liquidation committee on the administration of the estate, and the company's assets and liabilities. The information is typically communicated by way of detailed written report and accounts, which the liquidators also produce to the court.

As to whether creditors may pursue the estate's remedies against third parties, see the response to question 27.

### Enforcement of estate's rights

**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

Creditors are not permitted to pursue the estate's remedies themselves. They may, however, decide to provide the liquidator with funding to pursue the claim if they expect to benefit sufficiently from any recoveries that the liquidator may make. Any funding they provide would also be an expense of the liquidation, for which they would be reimbursed out of any assets in the estate before any distribution is made. Alternatively, where for example funding is unavailable or the claim is considered too risky, the liquidator might seek the court's permission to sell and assign the claim to a third party, who might then pursue it for his own benefit.

### Creditor representation

**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

The Winding Up Rules require a liquidation committee to be established in respect of every company that is being wound up by the court, though permitting the court to dispense with the requirement in particular cases. The committee will be composed of members, creditors or both, depending on whether the company is solvent, insolvent or of doubtful solvency: its composition will be determined by a vote of the creditors where the company is insolvent, members where it is solvent, and both where its solvency is doubtful (with a majority of creditors being elected). Any creditor will be eligible for appointment as long as

he has submitted a proof of debt that has not been rejected, and members (including beneficial owners of shares certified as such by their custodians or clearing houses) will be eligible for appointment.

Official liquidators are under a duty to report to the committee on matters that are of concern to it with respect to the winding up. Liquidators and committees typically meet regularly, and not less than semi-annually, and any two committee members can requisition a meeting. The committee will often be asked to approve certain matters by resolution (either by majority vote at a meeting or unanimously in writing) on which the liquidators propose to seek the court's permission, such as obtaining funding to pursue litigation, engaging legal counsel or other professionals, sales of property and payment of the liquidators' own remuneration.

The committee is entitled to engage a legal adviser, and the legal fees and expenses that the committee reasonably and properly incurs in obtaining legal advice will be paid out of the assets of the company as an expense of the liquidation.

### Insolvency of corporate groups

**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

While the insolvency proceedings relating to each group company must be commenced by a separate petition, the court will take a pragmatic approach to the management of the proceedings and may permit the proceedings to be dealt with together in appropriate cases.

Save where there are reasons for piercing the corporate veil (see the response to question 40), it will generally not be possible for the assets and liabilities of separate companies to be pooled for distribution purposes: one possible exception is where the affairs of the separate companies are so interwoven, and improperly and inadequately accounted for, that it would be impracticable or uneconomic to attempt to treat the companies separately and distinctly for the purposes of their liquidations. Where, however, a single Cayman Islands company has operations in various jurisdictions and there are liquidators appointed in one or more of those jurisdictions, then (subject to court sanction) a pooling arrangement may be entered into: ie, the assets realised in each jurisdiction may be aggregated and distributions to admitted creditors, pursuant to claims of creditors in the respective jurisdictions, are made from that pool of assets.

### Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

An order for the winding up of a company is treated as a final order and the respondents to the winding up petition will therefore have an automatic right of appeal against that order. Orders that are made in the course of, or by way of regulation of, a liquidation and any other orders that are ancillary to or consequential on a winding up order are, however, treated as interlocutory orders, and a party who wishes to appeal against any such order must, therefore, obtain permission to proceed with an appeal. The appellant is required to deposit CI\$50 with the Grand Court as security for the due prosecution of the appeal, and the court has a broad discretion to order the appellant to provide further security for the respondent's anticipated costs of the appeal. The amount of security which an appellant may be ordered to provide will be based on the anticipated costs, and, in deciding whether to make such an order, the court will have regard to, *inter alia*, the prospects of the appeal succeeding, the location of the appellant and the appellant's conduct in the proceedings, including its attitude to adverse costs orders made against it.

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**Claims**

- 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

A creditor must set out details of its claim on a proof of debt form and submit the form, together with any relevant documentary evidence, to the liquidator. Time limits are addressed in the response to question 38. The liquidator may admit the proof of debt, either entirely or in part, for a distribution, or he may reject it.

The liquidator must give the creditor notice of a rejection or admission of only part of its proof of debt, with the reasons therefor, and informing the creditor of its right to apply to the court for a reversal or variation of his or her decision. An application to the court will be made by summons within 21 days of the creditor receiving the notice, with supporting evidence.

Creditors are permitted to assign their rights to receive distributions to third parties or instruct the liquidator to pay them to third parties. Notice of an assignment would need to be given to the liquidator to enable the liquidator to pay the distribution to the assignee.

Claims for contingent and unliquidated amounts can be proved in a liquidation, and the liquidator adjudicating a proof for such a debt must consider the proof and supporting documents and make a just estimate of the value of the claim.

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**Modifying creditors' rights**

- 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

The court has no power to alter the rank of a creditor's claim, which is fixed by statute.

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**Priority claims**

- 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Apart from employee-related claims, debts due to bank depositors and taxes due to the Cayman Islands government will rank as preferred debts over those owed to other unsecured creditors. There is no type of unsecured claim that has priority over secured creditors.

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**Employment-related liabilities in restructurings**

- 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

Employees who are terminated as a result of a restructuring are often terminated for redundancy, which is a fair reason for dismissal under Cayman Islands employment law. The employer must however be seen to have acted reasonably in all the circumstances to avoid liability for unfair dismissal. It is wise to consult employees in advance of termination for redundancy in a restructuring, and employees terminated for this reason are entitled to notice and severance pay. Where employment is terminated by reason of a company going into liquidation, the law provides that the employee is entitled to severance pay. Severance pay is calculated as one week's wages at the employee's latest basic wage for each year of service the employee has completed, but legislative reforms are being considered that may increase the amount employers are required to pay in future cases.

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**Pension claims**

- 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

A company with employees in the Cayman Islands is generally required by law to contribute to their pensions: the employer and employee must

each contribute 5 per cent of the employee's earnings, though they may contribute more.

Employers typically assume responsibility for deducting and delivering their employees' contributions to the pension plan at the same time that they pay in their own. Where the employer has failed to pay its own contributions to the pension plan, it therefore tends to be the case that it has also failed to deliver its employees' contributions. Both classes of unpaid contributions will be held by the company on trust and will fall outside of the insolvency estate: undelivered employee contributions are held on trust for the employee and unpaid employer contributions are held on trust for the beneficiaries of the pension plan as a whole. The law additionally provides that the administrator of the pension plan has a lien and charge on assets of the employer in an amount equal to the amount of the unpaid contributions that it holds on trust, thus making the administrator a secured creditor.

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**Environmental problems and liabilities**

- 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

This is not a matter addressed by local legislation. It is, however, noted that claims in tort may lie against the company and possibly others who are responsible for causing environmental damage.

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**Liabilities that survive insolvency proceedings**

- 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

In the case of corporate insolvency, the debtor company will be dissolved once its affairs are completely wound up and any assets have been distributed. It is not possible for any liability of the debtor company to survive this process, since dissolution means that the debtor company has irreversibly ceased to exist.

In the case of a reorganisation by way of a creditors' scheme of arrangement, the scheme will set out the terms on which all liabilities to the creditors to which the scheme applies will be discharged. Once the scheme is approved by vote and receives court approval, its terms will bind all creditors and all liabilities to them will be discharged in accordance with the terms of the scheme.

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**Distributions**

- 38 How and when are distributions made to creditors in liquidations and reorganisations?**

A liquidator may declare an interim distribution to creditors when he determines that he has realised sufficient assets to be able to make the distribution. Upon making that determination, the liquidator is required to publish a notice of his or her intention to declare the distribution, fixing a date not less than 30 days from the date of publication by which proofs of debt must be lodged with him or her and stating that any creditor who lodges its proof of debt after that date will be excluded from the interim distribution but not from any subsequent interim or final distribution.

The liquidator is required to declare a final distribution once he has realised all of the company's assets, or so much of them as can be realised without needlessly protracting the liquidation, and divided any unrealised assets amongst the creditors in specie, if and to the extent that it was practical to do so. The liquidator is again required to publish a notice of his intention to declare the distribution, but, in this case, fixing a date not less than 60 days from the date of publication by which all proofs of debt must be lodged with him and stating that any creditor who lodges its proof of debt after that date may be excluded from the final distribution.

While the Winding Up Rules do not fix a deadline for the liquidator to adjudicate proofs of debt submitted for the purposes of an interim distribution, the liquidator is obliged to adjudicate proofs of debt submitted prior to the final date for lodging proofs of debt (fixed by the notice of his intention to declare a final distribution) within 14 days from the final date.

### Update and trends

The Cayman Islands has dominated in recent years as the offshore jurisdiction most popular for merger and consolidation activity. Despite the large amount of merger activity in the Cayman Islands over this period, to date just one fair value determination case (ie, where a shareholder dissenting from the merger requires the court to determine the fair value of its shares in a company that is part of the merger or consolidation) has proceeded to trial: see *In re Integra Group* (Jones J, 28 August 2015). The judgment in *Integra* provides welcome guidance on the meaning of 'fair value' under Cayman Islands law and its approach to expert valuation evidence. Since *Integra*, a number of further fair value proceedings have been commenced in the Cayman courts, so we may well see further jurisprudence in this area in due course.

For a number of years, the Cayman Islands has been considering enacting legislation to extend the reciprocal enforcement of foreign judgments under the Foreign Judgments (Reciprocal Enforcement) Law to jurisdictions beyond certain Australian states. As explained in the response to question 8, it presently remains the case that a party who has obtained judgment in a foreign court (other than the Australian courts) and wishes to enforce that judgment against assets situated in the Cayman Islands will rely upon well-established common law procedures to enforce the judgment. This is done by the judgment creditor issuing a claim for payment of the judgment debt in the Cayman court to obtain a Cayman judgment that can then be enforced against the assets in the Cayman Islands by the usual methods.

The manner and timing of distributions to creditors in a reorganisation by way of a scheme of arrangement will be determined by the terms of the scheme; similarly, the manner and timing of payments to members following a merger or consolidation will be determined by the plan of merger or consolidation.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

As indicated in the response to question 10, any disposition of the company's property and any transfer of shares or alteration in the status of its members made after the commencement of the winding up will, unless the court otherwise orders, be void. Additionally, where a company has made a payment or transferred property to a creditor while insolvent, and within the six months preceding the commencement of its insolvency proceedings, with the dominant intention to prefer that creditor over other creditors, the liquidator may ask the court to declare the payment or transaction void and to order that the payment be refunded or the property returned to the company (known as a voidable preference claim). The liquidator may also ask the court to declare a disposition of property by the company void where the company has disposed of the property at an undervalue with the intention of defeating an obligation owed to a creditor and seek an order for restitution (an undervalue claim). A creditor prejudiced by such a disposition may also seek such relief under the Fraudulent Dispositions Law whether or not insolvency proceedings have been commenced or are ongoing. The Grand Court has recently held that the usual defences to a restitutionary claim cannot be raised to defeat such statutory claims, and the point has been appealed to the Court of Appeal; its judgment is expected to be delivered shortly.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

As indicated in the response to question 39, one of the ingredients of a voidable preference claim is that the payment or transfer of property was made within the six months preceding the commencement of the relevant insolvency proceedings. This is commonly referred to as a look-back period in the Cayman Islands. Claims to avoid dispositions at an undervalue are not, however, subject to any look-back period.

The ability of a creditor to bring an undervalue claim under the Fraudulent Dispositions Law is addressed in the response to question 39. If a reorganisation by way of a creditors' scheme of arrangement is underway while the creditor has such a claim, the terms of the scheme should address the settlement of the claim.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Corporate officers and directors are not ordinarily liable for their corporation's obligations. It is, however, possible for them to assume responsibility for payment of particular liabilities by giving personal guarantees in respect of them. It is also possible for an officer or director to be declared liable to contribute to his company's assets where the court finds that he was knowingly a party to the company carrying on business with the intent to defraud its creditors or for some other fraudulent purpose.

Aside from this, where an officer or director acts in breach of the fiduciary duty or duty of care that he owes to his company, he may be held liable to compensate the company for any loss; alternatively, where he profits from a breach of fiduciary duty, he may be held liable to pay the profit to the company.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

A parent or affiliated corporation may be responsible for certain liabilities of a subsidiary or affiliate where it has given a guarantee to the creditor to whom those liabilities are owed. Absent a contractual assumption of responsibility for the payment of such liabilities, the parent or affiliated corporation might only be made responsible if it can be shown that it has abused the separate corporate personality of the subsidiary or affiliate to evade payment or frustrate the enforcement of those liabilities, such that the corporate veil of the subsidiary or affiliate can be pierced.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There is no restriction in insolvency proceedings on bona fide claims being made by insiders or non-arm's length creditors. The claim will be subject to proof in the usual way and the liquidator will need to be satisfied by the evidence that it is valid (both as to liability and as to the amount claimed), and take into account any claim which the company may set off against it, before admitting it for payment.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

A creditor will typically be permitted by the terms of its charge to appoint a receiver without needing to apply to the court, and the terms of the charge will determine the circumstances and manner in which the appointment may be made (typically by written notice to the chargor). Where the receiver is appointed over real property, notice of the appointment must however also be filed with the Registrar of Lands.

Where real property is let, a landlord may seize and sell property belonging to the tenant on the premises to set off the sales proceeds against unpaid rent. In the sale of goods context, where the contract for sale contains an effective title retention clause and the purchaser fails to pay for goods received, the clause may cause the purchaser to return the goods to the seller without requiring litigation to be pursued.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

There is no process other than a formal liquidation by which a company may be dissolved. While a company may cease to exist where the Registrar of Companies strikes it from the register of companies (either at the request of the company or of her own motion), unlike a dissolution, the striking off may be reversed by an order of the court up to 10 years after the company was struck.

Solvent companies often use the strike off process to bring their existence to an end where they are able to verify to the Registrar that they have no assets and liabilities, they consider the more formal voluntary liquidation process unnecessary and wish to save time and expense. The Registrar may also strike a company from the register of her own motion where she has reason to believe that it is no longer carrying on business or in operation, often because it has failed to pay its annual fees. Where a company has been struck from the register in either case, it will be open to the struck off company (acting by a former director) or a member of that company to apply to the court for an order restoring it to the register on the ground that it was in fact carrying on business or in operation at the time of the striking off, or that justice requires it to be restored. A creditor of a struck off company may also petition the court to restore the company and put it into liquidation. The effect of a restoration is that the company will be treated as never having ceased to exist.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

A liquidation case will be formally concluded when the company is dissolved. In the case of a voluntary winding up, the dissolution will follow the filing of the liquidator's return with the Registrar, and, in the case of a compulsory or court-supervised winding up, it will follow the filing of a court order for the company's dissolution.

A reorganisation by way of a scheme of arrangement will be concluded in accordance with the terms of the scheme. Where the scheme is a creditors' scheme that has been carried out in conjunction with the appointment of provisional liquidators to take advantage of the statutory moratorium on claims, it will, however, also be necessary to apply to the court for an order discharging the provisional liquidators and bringing the provisional liquidation to an end.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

Cayman law permits a representative appointed in foreign bankruptcy proceedings to apply to the court for orders in aid of foreign insolvency proceedings. Where the court is willing to exercise its discretion, it may:

- grant the foreign representative recognition (power to act in the Cayman Islands);
- enjoin the commencement or stay the continuation of legal proceedings against the debtor;
- stay the enforcement of any judgment against the debtor;
- require a person in possession of relevant information to be examined and produce documents; and
- order the delivery up to the foreign representative of any property belonging to the debtor.

While the Cayman Islands is not a signatory to any treaty on international insolvency, the court is willing to exercise its powers in aid of foreign proceedings based on comity. These powers and the basis on which they will be exercised follow many of the principles enshrined in the UNCITRAL Model Law, but stop short of implementing it.

Foreign creditors are treated the same as local creditors. The enforcement of foreign judgments is addressed in the response to question 8.

### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

In the Cayman Islands, there are no threshold tests for the grant of assistance in respect of foreign insolvency proceedings, or automatic rights based on the COMI of the debtor. The foreign representatives must satisfy the court that it is appropriate for it to exercise its discretion to grant the relief sought by their application.

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**Cross-border cooperation**

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**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

With respect to recognition, see the response to question 47. The court is willing to cooperate with foreign courts and foreign representatives in cross-border insolvencies based on comity, a consequence of which is that it is possible that the court may refuse to grant recognition or other assistance where to do so would be materially inconsistent with Cayman Islands law and contrary to public policy.

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**Cross-border insolvency protocols and joint court hearings**

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**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

In any case where a company in liquidation or its assets are subject to bankruptcy proceedings in another jurisdiction, a Cayman liquidator is required to consider whether it would be appropriate to enter into a cross-border protocol with any relevant foreign representative. The court may authorise cross-border protocols requiring the pooling of assets, information sharing and allocation of responsibility between liquidators to ensure fairness, efficiency and costs savings.

The court in appropriate cases may communicate or hold joint hearings with courts in other countries, and has previously done so with courts in, for example, England, the United States and Luxembourg.

# China

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Enterprise Bankruptcy Law of the People's Republic of China (the EBL) is the legislation principally applicable to the insolvencies and reorganisations of all 'enterprise legal persons' incorporated in the People's Republic of China (the PRC). The EBL could also apply by reference to bankruptcy liquidation of 'non-enterprise legal persons' (such as private schools).

The Supreme People's Court from time to time issues judicial interpretation specific to practical problems arising from implementation of the EBL. So far the Supreme People's Court has issued two important judicial interpretations for the EBL (ie, the Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the PRC issued on 9 September 2011 (the 2011 Interpretations) and the Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the PRC II issued on 5 September 2013 (the 2013 Interpretations)).

As well as judicial interpretations, which usually cover a number of key questions, the Supreme People's Court also issues opinions in the form of formal reply to a lower court's question in a particular case. Those replies and opinions are considered as supplemental mandatory sources in practice.

At local court level, some courts have their special rules or guidelines for the administrator, usually from a procedural perspective. Such rules or guidelines would also restrict or affect the debtor or creditor's right to a certain extent.

A debtor is insolvent when it is unable to pay its debts when due and its assets are insufficient or it lacks the ability to clear its debts. The debtor needs to prove either of the foregoing situations exists if it voluntarily initiates the bankruptcy liquidation by filing an application. However, if a creditor petitions to have its debtor placed in bankruptcy, it only needs to show that the debtor is unable to pay its debts when due and payable. Also when a debtor under liquidation finds that its assets are insufficient to clear its debts, the obligation to apply for bankruptcy liquidation is triggered.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The PRC does not have a court that deals solely with bankruptcy cases. Usually those cases are heard by the civil or economic division of a court. However, the Supreme People's Court has launched a programme in June 2016, under which intermediate courts in certain cities are required to set up a liquidation and bankruptcy division to exclusively hear liquidation and bankruptcy-related cases.

The court of the place where the debtor is domiciled has jurisdiction over the debtor's bankruptcy case. The domicile of a debtor is the place of its head office or place of main business. However, in practice, the place where the debtor registers its business would usually be deemed its domicile.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The EBL could apply by reference to bankruptcy liquidation of 'non-enterprise legal persons'. In 2011, the Supreme People's Court made it clear that the EBL may apply by reference to sole proprietorships but the creditor may claim against the investor of the sole proprietorship for debts or other claims that remain unpaid even after the liquidation of the sole proprietorship. Bankruptcy of a natural person is not available in the PRC legal system.

All the assets of the debtor at the time that the court accepts the bankruptcy application and the assets acquired by the debtor after the acceptance are the debtor's assets, including, among other things, intellectual property, equity and credit against third parties. After the debtor is declared bankrupt by the court, the debtor's assets will constitute its bankruptcy estate. However, those assets that belong to a third party but are placed in the debtor's possession arising from, for example, lease, storage and consignment arrangements or agreements, are not the debtor's assets.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The EBL is applicable to state-owned enterprises, with the only exception that, bankruptcy proceedings of certain state-owned enterprises, as approved by the State Council before the implementation of the EBL, could follow grandfathering rules formulated by the State Council. However, as far as we know, there remain no such state-owned enterprises which are yet to be liquidated according to the grandfathering rules.

Pursuant to the Law of the People's Republic of China on the State-Owned Assets of Enterprises, when applying for bankruptcy against themselves, wholly state-owned enterprises shall obtain decision by the authorities/organisations playing shareholders' roles; significant wholly state-owned enterprises and state-controlled companies shall obtain approval by the government of the same level; and state-invested enterprises shall consult trade unions and employees for their opinions.

In addition, disposal of assets during the bankruptcy proceedings of state-owned enterprises may undergo certain special examination and approval procedures.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

In the PRC, financial institutions principally include commercial banks, securities companies and insurance companies, and are subject to regulations by different regulatory authorities. The regulatory authority for commercial banks is the China Banking Regulatory Commission (CBRC), for insurance companies, the China Insurance Regulatory Commission (CIRC) and for securities companies, the China Securities Regulatory Commission (CSRC).

Bankruptcy of financial institutions is subject to special rules. The EBL generally provides that a relevant regulatory authority may apply to the court for bankruptcy or reorganisation of an insolvent financial institution under its supervision. Where a regulatory authority temporarily takes over management control of a financial institution in serious operational risk, the regulatory authority can apply to the court to suspend all the civil litigation or enforcement proceedings against the financial institution. The State Council may promulgate rules for bankruptcy of financial institution in accordance with the EBL and other laws.

Under the Law on Commercial Bank of the PRC, when a commercial bank has suffered or will probably suffer from credit crisis, thereby seriously affecting the interests of the depositors, the banking regulatory authority under the State Council (ie, the CBRC) may assume control over the bank. Also, if a commercial bank is unable to pay its debts when due, the court shall declare bankruptcy of the bank upon the CBRC's approval. After the bank is declared bankrupt, the court shall appoint relevant authorities, such as the CBRC, and relevant persons to establish a liquidation group to carry out liquidation. In distribution, an individual's claims for principal of savings deposits and interest thereon shall be given priority after the liquidation expenses, the wages owed to the employees and the labour insurance premiums have been paid.

According to the Securities Law of the PRC, during liquidation (including bankruptcy liquidation) of a securities company, with the approval by the CSRC, directors, supervisors or senior managers who are directly accountable to the company and other persons who are directly responsible can be subject to border control or be prohibited from transferring or disposing of their property or creating encumbrances on the property.

The Insurance Law of the PRC provides, where an insurance company is insolvent, upon the approval of the insurance regulatory authority under the State Council (ie, the CIRC), the insurance company or its creditor may apply to the court for reorganisation, conciliation or bankruptcy liquidation; the CIRC may also apply to the court for reorganisation or bankruptcy liquidation of the insurance company. In distribution, claims for indemnity or payment of the insurance benefits shall be given priority after the costs for bankruptcy proceedings, debts for common benefit and certain employment-related claims have been paid (see question 34).

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### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

Mortgage is the most common security interest created over real property. A mortgage over buildings (including those still under construction) must be created at the same time over the underlying land-use rights; building and its land-use right cannot be mortgaged separately unless no building exists on the land. The land itself, or more precisely ownership of the land, cannot be mortgaged. This is because in PRC, ownership of land in urban areas lies solely in the state and land in rural areas belongs to village collectives. Other than the state and village collectives, the other entities can only have the right to use the land for a fixed term.

The contract of mortgage over real property must take the form of written agreement and mortgage is established and effective upon registration with the appropriate authorities.

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### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

Principal types of security created on moveable (personal) property include mortgage, pledge and lien.

Mortgage over moveable property does not require delivery of possession of the property; the owner still possesses the property (as opposed to pledge). A floating mortgage may be created by a company, individually-owned business or agricultural operator over all its existing and future production equipment, raw materials, semi-finished products and finished products. Mortgage over moveable property, including floating mortgage, also requires a contract in writing but is established at the time the mortgage contract comes into force (as opposed to mortgage on real property). However, the mortgage is not effective against a third party unless it is registered with relevant authorities.

Pledge over moveable property requires delivery of possession of the property. A pledge contract must take the form of written agreement and the pledge is established at the time of delivery of possession of the property.

In addition to moveable properties, a pledge can also be created over negotiable instruments (for example, money order), documents of title (for example, bill of lading), equity interest, registered intellectual property rights and account receivables.

Liens are statutory rights that allow the creditor to continue to retain the debtor's property when the debtor is in default. Property retained under the lien between companies do not need to be within the same legal relationship of the claim or debt. In terms of ranking, right of lien is superior to mortgage or pledge existing over the same property, even if the mortgage and pledge have been created prior to the lien. Right of lien perishes when the creditor no longer possesses the property.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Once the court accepts the bankruptcy application, all existing preservation measures taken against the debtor's assets in all civil proceedings are lifted and all the civil litigation, arbitration and enforcement proceedings are suspended. Unsecured creditors have no further remedies other than those available within the bankruptcy procedures.

However, before the court officially accepts the bankruptcy application, the creditor can initiate an action against the debtor and apply for preservation measures within the litigation. In practice, the court would often ask the applicant to provide security for its application for preservation measures, although security is not mandatory under the Civil Procedures of the PRC for application made during an ongoing litigation. If the applicant refuses to provide security, the court will reject the application. The creditor can apply for preservation measures before it starts the lawsuit if it can show that it would suffer irreparable harm should the preservation measures not be taken immediately. In this scenario, the court must request the applicant to provide security. If the applicant fails to provide security, its application will be rejected. The court must issue a ruling within 48 hours after it receives the application. A successful applicant must lodge the lawsuit within 30 days after the court takes preservation measures; otherwise, the measures shall be stopped.

The form of security acceptable to courts would vary from court to court because a particular court has discretion in deciding what security is acceptable to it. However, a cash deposit will usually suffice. Preservation measures against property generally include sealing-up, seizure and freezing of bank accounts.

Discharge made in litigation (including court mediation), arbitration or enforcement proceedings are exempted for annulment even if the discharge has occurred within six months before the court accepts the bankruptcy application, unless the debtor and creditor maliciously act together to undermine the interest of the other creditors (see question 39).

However, a case involving a foreign party is a foreign-related action under the Civil Procedures of the PRC and hence is not subject to the time limit set up for trials of domestic cases (ie, six months for first instance proceedings and three months for the appellate proceedings). That makes it difficult to predict how long the proceedings will last and once the application for bankruptcy is accepted, all pending civil proceedings will be stayed.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A debtor may apply the court for bankruptcy liquidation if:

- it is unable to pay its debts when due and its assets are not sufficient to clear its debts; or
- it is unable to pay its debts when due and obviously lacks the ability to clear its debts.

The Supreme People's Court further explains the rules in the 2011 Interpretations.

- The debtor is unable to pay its debts if the following three elements are met at the same time:
  - the creditor–debtor relationship is legally founded;
  - the payment is due and payable; and
  - the debtor fails to fully discharge the debt.
- The debtor’s assets are not sufficient to clear its debts if its balance sheet, auditing report or asset evaluation report so indicates, unless there is evidence to the contrary.
- The debtor obviously lacks the ability to clear its debts even when the book value of its assets still exceeds its liabilities, if one of the following situations exists:
  - the debtor is unable to repay the debt because of cash flow or liquidity reasons;
  - the debtor is unable to repay the debt because the legal representative or other responsible person’s whereabouts are unknown;
  - discharge is still impossible even after the court’s compulsory enforcement; or
  - the debtor is unable to repay the debt because of chronic losses and to turn around the business would be difficult.

To file a voluntary liquidation application the debtor must submit to the court a written application and supporting evidence including, among other things, a description of assets, list of debts, list of credits, financial statements, employee settlement plan and description of the status of payment of salaries and social insurance expenses for the employees. In practice, the court will sometimes issue an initial acceptance and designate a time period for the debtor to settle certain outstanding issues before it officially accepts the case.

After the court formally accepts the bankruptcy application, all the pending civil litigations or arbitrations with respect to the debtor should be suspended until the administrator takes over the debtor’s assets; all the preservation measures taken against the debtor’s assets should be lifted and enforcement proceedings be suspended. All the civil litigations with respect to the debtor, which are filed after the court accepts the bankruptcy application, should be filed to the same court hearing the bankruptcy case.

The court will appoint an administrator to take over and manage the debtor’s assets. The administrator will decide whether to continue or suspend the debtor’s business operation, subject to the court’s approval. This power would lie in the creditors’ meeting after its formation. The administrator will also decide whether to continue or terminate a contract that has been formed before the acceptance of the bankruptcy case but has not been completely performed. The other party can ask for security if the administrator decides to continue performing the contract. The contract shall be deemed terminated if the administrator refuses to provide security, fails to notify the other party of its decision within two months of the court’s acceptance of the bankruptcy, or fails to reply to the other party’s demand within 30 days.

### **Involuntary liquidations**

#### **10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

The criteria are much less stringent for a creditor to apply for liquidation of its debtor. The creditor only needs to show that the debtor is unable to pay its debts when due. To do that, the creditor should submit to the court a written application together with supporting evidence. After the court receives the petition, it will notify the debtor within five days. The debtor will then have seven days to lodge an objection and the court will decide whether to accept the creditor’s application within 10 days after the prescribed period for objection expires. If the debtor does not object or its grounds for objection cannot stand, the court will accept the application.

In practice the court will usually require the creditor to produce evidentiary documents such as a binding judgment or arbitral award, especially when the debtor challenges the credit.

The 2011 Interpretations made it clear that the argument that a third party jointly liable for the debt still has the ability to pay is not a valid defence. After acceptance, the court will order the debtor to provide a description of its financial status, list of debts, list of credit and financial statements, and has the power to impose penalties on the person directly responsible if the debtor refuses to follow the order.

The effects of involuntary liquidations are the same for voluntary liquidations (see question 9).

### **Voluntary reorganisations**

#### **11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

A debtor may petition the court for reorganisation if:

- it is unable to pay the debt when due and its assets are not sufficient to clear all its debts;
- it is unable to pay the debt when due and obviously lacks the ability to pay; or
- there is an obvious likelihood that it would lose its ability to pay in the future.

In the event that a court accepts a creditor’s application for bankruptcy liquidation against the debtor, the debtor still has the chance to convert the bankruptcy liquidation into bankruptcy reorganisation by filing a petition, but the petition for reorganisation should be raised before the court declares bankruptcy of the debtor. Besides the debtor, shareholders of the debtor holding 10 per cent or more of the debtor’s equity may also apply for reorganisation.

During reorganisation, the administrator is responsible for managing the assets and running the business, but it can hire the debtor’s management to do so. The court can approve the debtor to manage the assets and operate the business under the administrator’s supervision, upon the debtor’s request.

After the court decides that the debtor should undergo reorganisation, the debtor (or the administrator in the event that the administrator manages assets and operates business during reorganisation) should propose a draft plan for reorganisation. Once the draft plan is approved and adopted, it shall be binding over the debtor and all the creditors.

Enforcement of security interest by the creditors shall be stayed, unless the creditor applies for exemption from the stay if there is risk of damage to the collateral or significant decrease in the value of the collateral.

Moreover, during reorganisation, shareholders of the debtor are not allowed to request profit distribution. And unless approved by the court, the debtor’s director, supervisor and senior managers cannot transfer their equity, if any, in the debtor to any third party.

### **Involuntary reorganisations**

#### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

The requirements for a creditor to petition for reorganisation of its debtor and the thresholds for it to apply for bankruptcy liquidation of its debtor are the same, namely, the creditor needs to show that the debtor is unable to pay the debt when due and payable.

The effects of involuntary reorganisations are the same as per voluntary reorganisation.

### **Mandatory commencement of insolvency proceedings**

#### **13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

The EBL does not provide for circumstances that would obligate the debtor or its responsible person to commence insolvency proceedings except that in the event of non-bankruptcy liquidations, if the person responsible for liquidation finds that the company’s assets are insufficient to clear the company’s debts, it has the duty to petition for bankruptcy to the court. The Company Law of the PRC imposes similar obligation over the liquidation committee in non-bankruptcy liquidation.

In enforcement proceedings, if an enforcement court finds that the enterprise subject to enforcement is unable to pay its debts when due and its assets insufficient to clear its debts, or is unable to pay its debts when due and obviously lacks the ability to clear its debts, the court shall, upon consent of one of the enforcement applicants or of the enterprise subject to enforcement, suspend the enforcement proceedings and transfer the case to the court of the place where the enterprise

subject to enforcement is domiciled for the latter court to decide whether to accept the case as a bankruptcy case.

Directors, supervisors and senior managers of a company generally owe fiduciary duties toward the company, which include the duty of loyalty and the duty of due diligence. Under the EBL, directors, supervisors and senior managers are liable if they breach their fiduciary duties, which results in the bankruptcy of the company.

### Doing business in reorganisations

- 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

After an application for reorganisation is voluntarily or involuntarily filed against the debtor and before a reorganisation plan is approved, the administrator can operate the business or the debtor, upon request to and approval by the court, can carry out the business under the administrator's supervision. After the reorganisation plan is approved, the plan will be implemented by the debtor under the administrator's supervision during the supervision period.

In the event of reorganisation, before the reorganisation plan is approved, sale of assets is subject to the creditors' meeting's approval or, before the creditors' meeting is established, shall be reported to the court. After the plan is approved, sale of the assets of the business shall be under the administrator's supervision. Claims arising from provisions of goods or services to the debtor after the filing are usually treated as priority claims of debts for common benefits. The court will supervise the debtor's business activities through the administrator.

No special power is endowed with the directors or officers after insolvency proceedings are commenced. If the debtor is approved to run the business, its directors and officers may exercise the powers that are generally available to a director or officer of a company, subject to the administrator's supervision or any resolution adopted by the creditors' meetings or any reorganisation plan, depending on the specific scenario.

### Stays of proceedings and moratoria

- 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

After the court accepts the bankruptcy application, all the pending civil litigations and arbitrations should be stayed until the administrator takes over the debtor's assets. All the preservation measures taken against the debtor's assets should be lifted and the enforcement procedures suspended.

Under the EBL, the administrator is required to provide alternative security or to repay the debt if it wants to repossess the assets that are in the possession of a creditor subject to a pledge or lien. If the administrator chooses not to repossess the assets, the pledger or lien holder is entitled to dispose of the assets in accordance with the statutory procedures.

In reorganisation, a secured creditor's right to enforce its security interest is stayed unless it successfully pleads for exemption from the stay by showing to the court that there is a risk of damage to the collateral or obvious depreciation in value of the collateral, which would damage the right of the creditor.

### Post-filing credit

- 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

For post-filing financing, the EBL clearly provides that during reorganisation, the debtor (if approved by the court to continue managing the assets and operating the business) or the administrator may borrow loans and create security over the debtor's assets to secure the loans for the purpose of continuing the business. Such post-filing credits are usually treated as priority claims of debts for common benefits.

In bankruptcy liquidation, the administrator can obtain secured and unsecured loans but should timely report the actions to the creditors' committee or to the court if there is no creditors' committee. Before the first creditors' meeting is held, the administrator should obtain the court's approval if it decides to borrow loans and create security. Those post-filing credit are usually treated as priority claims of debts for common benefits.

### Set-off and netting

- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

A creditor can exercise its right of set-off for mutual debts that have arisen before the court accepts the bankruptcy application, with the following exceptions:

- the claim cannot be set off if it is obtained by the creditor from a third party after the acceptance of the bankruptcy application; and
- the claim cannot be set off if at the time the credit or debt was created, the creditor knew that the debtor was insolvent or had applied for bankruptcy unless the credit or debt was mandated by law or because of a cause that occurred more than one year before the application for bankruptcy.

The above exceptions do not apply to secured creditors if the secured claim setoff does not exceed the value of the collateral.

Certain claims of the debtor against its shareholder are not permitted to be set off. One is claim for outstanding capital contribution and the other is the claim for damages because of the shareholder's abuse of shareholder's right or interested transactions.

### Sale of assets

- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

Whether it is a sale of specific assets out of the ordinary course of business or the sale of the entire business of the debtor, which rarely happens in reorganisation cases, the sale should comply with the duly approved reorganisation plan. In bankruptcy liquidation, disposition of assets must follow the disposition plan adopted by the creditors' meeting and approved by the court and sales of assets must be implemented through auction unless the creditors' meeting resolve otherwise or the law requires otherwise. From the perspective of the purchaser, it will acquire the assets 'free and clear' of claims.

The EBL is silent as to whether 'stalking horse' bids or credit bidding is allowed.

Credit bidding is not available under the EBL.

### Intellectual property assets in insolvencies

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

Whether an IP licensor or owner has the unilateral right to terminate the licence agreement when the debtor's insolvency case is opened primarily depends on what is agreed on in the agreement. Absent agreement, the EBL allows the administrator to decide whether to continue or terminate an agreement that has been formed before the acceptance of the bankruptcy case but has not been completely performed.

If the administrator elects to terminate the agreement, the IP licensor or owner may register the losses it suffers from the termination as credit. If the administrator decides to continue to perform the agreement, the IP licensor or owner may ask for security. The agreement

shall be deemed terminated if the administrator refuses to provide security, fails to notify the IP licensor or owner of its decision within two months of the court's acceptance of the bankruptcy, or fails to reply to the IP licensor or owner's demand within 30 days.

When the IP licensor or owner continues to perform the agreement upon the administrator's request, the claims for loyalties and other payments incurred thereof would be debts for common benefit and would be paid after secured claims and costs of bankruptcy proceedings but prior to any other claims.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

If the company legitimately collects the information, even when it becomes insolvent, the said company is still allowed to lawfully use such information.

However, under the Criminal Law of the PRC, one should be accountable for criminal liabilities for sale or provision of personal information of the citizens to others, with serious penalties if in violation of relevant provision of the PRC. It is not clear whether transfer or sale of personal information in bankruptcy liquidation or reorganisation would constitute an exception. It remains to be tested and clarified in future how the court would consider and treat the issues.

In addition, the collection and use policy that the company uses when collecting the information from its customers may also restrict the use or sale of the information.

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### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

The EBL does not specifically provide for the right for the debtor to reject or disclaim an unfavourable contract except for those contracts that are void or voidable (see question 40). However, an administrator in reorganisation is entitled to terminate any contracts formed before the acceptance of the bankruptcy case, without any cause, no matter whether such contracts are favourable or not.

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### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Arbitration cannot be used for insolvency proceedings. After the court accepts the bankruptcy application, all the pending civil litigations and arbitrations with respect to the debtor should be suspended until the administrator takes over the debtor's assets.

It is not clear under the EBL whether disputes that arise after the insolvency case is opened are allowed to be arbitrated even with the parties' consent. The EBL only provides that all the civil litigations with respect to the debtor, which are lodged after the court accepts of the bankruptcy application, should be filed to the same court hearing the bankruptcy case.

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### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

A reorganisation plan must include, inter alia, the following:

- a business plan of the debtor;
- a classification of the creditor's right;

- an adjustment plan of the creditor's right;
- a repayment plan of the creditor's right;
- the term for implementing the reorganisation plan; and
- the term for supervising the performance of the reorganisation plan.

For the purpose of a reorganisation plan, the creditors shall be classified into certain voting groups: secured creditors, employees, tax creditors, ordinary unsecured creditors, ordinary unsecured creditors of small amounts if the court deems it necessary and shareholders if the plan involves adjustment of the shareholders' interests.

The plan is passed by the creditors only when the plan has been passed by each of the above voting groups. And for a particular voting group, the plan is passed only when at least half of the creditors of that group present in the meeting vote for the plan and total credits of the creditors approving the plan of that group are equal to at least two-thirds of the total credits of that group. After the plan is passed on the creditor's level, the court will then examine and adopt the plan. However, the court will still adopt a plan if some requirements are met even when the plan is not passed by the creditors. The reorganisation plan approved by the court is binding over the debtor and all the creditors.

The EBL does not address the issue of releasing non-debtor parties from liability.

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### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

The concept of 'expedited reorganisations' is not available under the EBL. However, the parties may expedite the reorganisation through conciliation. A conciliation plan, which should be proposed by the debtor, is passed when at least half of the creditors present in the meeting vote for the plan and total credits of the creditors approving the plan are equal to at least two-thirds of the total unsecured credits. After the plan is passed on the creditor's level, the court will then examine and adopt the plan. The conciliation plan approved by the court is binding over the debtor and all the conciliated creditors. 'Conciliated creditors' refer to those unsecured creditors at the time the court accepts the bankruptcy application. Only the debtor is allowed to apply for conciliation; the creditor is not allowed to trigger this option.

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### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

The creditors could fail to pass the plan or the court may disapprove the plan. In either case, the court should terminate the reorganisation and declare bankruptcy of the debtor.

If the debtor fails to perform the plan, the court should, upon the request by the administrator or other interested party, terminate the reorganisation plan and declare bankruptcy of the debtor. The creditors' commitments over credit adjustments as made in the plan are no longer effective but the debtor's repayments made under the plan are still valid and could be retained by the creditors. The claims that remain unpaid will become bankruptcy claims.

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### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The court should send notice to the known creditors and make a public announcement within 25 days after it accepts the bankruptcy application. The notice and announcement should specify, among other things, the applicant, the debtor, date of acceptance, deadline for declaring credits, name and address of the administrator, time and place for the first creditors' meeting, demands for return of the debtor's property or for payment of debts owed to the debtor.

The first creditors' meeting is called by the court and should be held within 15 days after the period for declaring credits has expired. The court should allow a minimum of 30 days and a maximum of three

months for creditors to declare their credits. Subsequent meetings may be held by the court when it deems necessary. The administrator, the creditors' committee or the creditor (or creditors) holding at least a quarter of the total credits may call a meeting by proposing to the president of the creditors' meeting, who is appointed by the court from those creditors with voting right. For convening a creditors' meeting, the administrator should notify the known creditors at least 15 days in advance.

The EBL does not clearly stipulate what information should be made available to the creditors and when. In practice, the information available to the creditors may vary from case to case and the administrator may sometimes circulate the information or document for resolution merely a few days before the meeting, making it difficult for a creditor to make a meaningful decision before or during the meeting.

The administrator must be present at the creditors' meeting, report its performance of duties and answer queries from the creditors. The administrator should accept the supervision by the creditors' meeting and by the creditors' committee, and should timely report to the creditors' committee or to the court where the creditors' committee is not established, when taking certain actions of material effect.

The administrator is under the duty to recover the debtor's estate and to pursue a third party for return of property or for repayment of debt, but the creditor may directly sue a third party for the estate in some exceptional occasions (see question 27).

The EBL does not provide for release of liabilities owed by third parties. Therefore liabilities owed by third parties could not be discharged by implementation of the reorganisation plan.

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#### Enforcement of estate's rights

##### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

If the administrator fails to void certain voidable transactions (ie, transfer of assets free of charge, transaction at an obviously unreasonable price and waiver of creditor's claims), the creditor can enforce its right of annulment provided under the Contract Law of the PRC and request the court to annul the transactions (see also question 40). In this case, the fruits will go the debtor's estate.

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#### Creditor representation

##### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The creditors' meeting may decide to establish a creditors' committee. The committee will have at most nine members, which should include creditor representatives as appointed by the creditors' meeting and one employee representative of the debtor or one representative from its labour union. The creditors' committee shall supervise the management and disposition of the debtor's assets by the administrator, supervise the distribution of bankruptcy estate, call a creditors' meeting and undertake the other responsibilities as entrusted by the creditors' meeting.

The creditors' meeting has the power to appoint and replace the creditor representatives of the creditors' committee, subject to written endorsement by the court.

The EBL is silent as to whether the creditors' committee may retain advisers, but in practice the creditors' committee in some high-profile bankruptcy proceedings may retain outside advisers. The expenses for retaining the advisers shall be funded by the creditors' committee or in the way agreed by the creditors.

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#### Insolvency of corporate groups

##### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

The EBL does not address the issue of consolidation of bankruptcy proceedings. In practice, if the assets and liabilities of a series of affiliated

companies are highly mingled with each other, the court may allow combination of their bankruptcy proceedings. In such a scenario, the assets and liabilities of such companies will be pooled for distribution purposes.

The PRC court may recognise and enforce a judgment or verdict made by a foreign court in insolvency proceedings when certain criteria are met (see question 49). However, if a domestic bankruptcy proceeding of a related entity is already in place, it remains to be seen how the court would decide under this scenario.

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#### Appeals

##### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Where a court rules to decide not to accept an application for bankruptcy, the applicant may file an appeal against the ruling with the court at the next higher level within 10 days of the date the ruling is served. After the court accepts an application for bankruptcy but before it declares bankrupt of the company, if the court finds the company not insolvent, it may rule to reject the application. The applicant may file an appeal against the ruling with the court at the next higher level within 10 days of the date the ruling is served.

No permission is required for the appellant to appeal against the above rulings; neither is security required for filing the appeal.

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#### Claims

##### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

The creditor must declare its credit within the period as stipulated by the court in the notice or in the public announcement. In the declaration, the creditor should clearly indicate the amount of its credits and type of its credits (secured or unsecured), and provide supporting evidence. Failing to meet the deadline, the creditor is still permitted to make supplemental declaration before the final distribution but no supplemental distribution will be made for the distribution that has happened before the creditor's declaration.

The administrator is responsible for reviewing and confirming the creditor's credits. It will review the supporting documents provided by the creditor, examine the debtor's financial statements and other books and records, and prepare a list of credits for examination by the creditors' meeting. If the administrator or the creditor objects to the list, it may file an action with the court that accepts the bankruptcy application.

The EBL provides some restrictions over transferred claims (see question 17).

The creditor may declare contingent or unliquidated credits but it is not clear how the amounts of such claims are determined. Unmatured claims will be deemed matured at the time the bankruptcy application is accepted and interest shall cease accrual at the time of the acceptance.

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#### Modifying creditors' rights

##### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The court is not allowed to modify the rank provided under the EBL and distribution must comply with the statutory rank.

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#### Priority claims

##### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

A secured creditor is secured up to the value of the collateral. If the proceeds of collateral are not enough to pay off the debt, the unrepaid portion shall be treated as ordinary unsecured claims.

The costs of bankruptcy proceedings should be paid first, including litigation fee of the bankruptcy case; expenses for managing, disposing and distributing the debtor's assets; and expenses for the administrator's performance of duties, remuneration to the administrator and expenses for its recruitment for the bankruptcy proceedings. If the debtor's assets are not sufficient for paying off the expenses for bankruptcy proceedings, the administrator should apply the court to conclude the bankruptcy procedures. Debts for common benefit should be paid next to the costs of bankruptcy proceedings, followed by certain employment-related claims and then by certain social security premiums and taxes. The remainder, if any, shall be distributed to unsecured creditors.

#### Employment-related liabilities in restructurings

##### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Under the Labour Contract Law of the PRC, an employee is entitled to monetary compensation when terminated by a company. However, neither the EBL nor the Labour Contract Law provides special procedures for terminating an employee during restructuring or liquidation or requires an increase in the employee claims when large numbers of employees are terminated or where the business ceases operations.

Employment remuneration, social security premium and other employment-related claims incurred during the bankruptcy proceedings for the purpose of continuing the business are part of debts for common benefit and will be paid only after secured claims and costs of bankruptcy proceedings in distribution (see also question 33). Salaries, medical and disability subsidies, elementary retirement and medical payment payable to employees' individual accounts, and other monetary compensation required by law and regulation will be paid after the debts for common benefit, followed by other social security premiums and taxes.

#### Pension claims

##### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Pension-related claims rank third to fifth depending on the classifications of the claims and the time the claims arise (see questions 33 and 34). Employer-funded defined benefit pension schemes do not exist in China, so the question of actuarial deficiencies in pension funds does not therefore arise.

#### Environmental problems and liabilities

##### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The EBL does not address this issue.

#### Liabilities that survive insolvency proceedings

##### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

In bankruptcy liquidation, the debtor's liabilities will not survive the insolvency proceedings. In reorganisation, a creditor that fails to declare its credits in compliance with the EBL cannot enforce its rights during the implementation of the reorganisation plan. After that, however, it is allowed to enforce its rights subject to the same conditions (as provided in the reorganisation plan) as the other creditors of the same class.

#### Distributions

##### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In liquidation, distribution should be conducted according to the disposition plan and distribution plan as passed by the creditors' meeting and further approved by the court. Sales of assets must be implemented through auction unless the creditors' meeting resolve otherwise or the

law requires otherwise. Bankruptcy estate should be distributed in monetary form unless the creditors' meeting resolves otherwise.

In reorganisation, the reorganisation plan approved by the court is binding over all the creditors. Therefore, the creditors' claims will be partially or fully discharged in accordance with the reorganisation plan.

#### Transactions that may be annulled

##### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

Under the EBL, the following actions or transactions could be annulled if they have occurred within one year before the court accepts the bankruptcy application:

- transfer of assets free of charge;
- transaction at an obviously unreasonable price;
- providing security for unsecured debt;
- discharge of debt before it is due (not voidable if the debt later becomes due before the acceptance); and
- waiver of creditor's claims.

If the debtor, when insolvent, repays individual creditors within six months prior to the date when the court accepts the bankruptcy application, the administrator may request the court to annul such repayments, unless the individual repayment benefits the debtor's assets. Payments of water, electricity and other utility fees necessary for the basic operation of the debtor, salary payment and payment for damages because of personal injury are exempted and cannot be invalidated.

Moreover, individual repayment of secured debt for which the debtor provides its own assets as collateral is exempted from annulment, as long as the value of the collateral is higher than the debt owed by the debtor. Repayment made in litigation, arbitration or enforcement proceedings are also exempted unless the debtor and creditor maliciously act together to damage the interests of the other creditors.

Certain types of actions are invalid, rather than merely voidable. Those actions are: concealment and transfer of assets for the purpose of evading debts; and fabricating debts or admitting debts that do not exist.

After the related transactions are annulled, the related creditors should return their proceeds received from the transactions to the debtor's estate.

#### Proceedings to annul transactions

##### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

Under the EBL, the suspect period is one year for certain types of actions. To be specific, the administrator may request the court to annul the following actions that have occurred within one year before the court accepts the bankruptcy application:

- transfer of assets free of charge;
- transaction at an obviously unreasonable price;
- providing security for unsecured debt;
- discharge of debt before it is due; and
- waiver of creditor's claims.

Within six months before the court accepts the bankruptcy application, if the debtor has repaid individual debt when it is insolvent, the administrator may request the court to annul such repayments, unless such individual repayment benefits the debtor's assets.

In general, it is the administrator's power and responsibility to request the court for annulment. However, the creditor may claim liability against the administrator if the latter fails to enforce its right of annulment and hence diminishes the value of the assets. In addition, as clarified in the 2013 Interpretations, if the administrator fails to void certain voidable transactions (ie, transfer of assets free of charge, transaction at an obviously unreasonable price and waiver of creditor's claims), the creditor is allowed to exercise its right of annulment provided under the Contract Law of the PRC even in a bankruptcy scenario.

Avoidance actions may be attacked in both a reorganisation and a liquidation.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Corporate officers and directors are generally not liable for their corporation's obligations unless they breach their fiduciary duties and cause the damages. Under the EBL, directors, supervisors and senior managers are liable if they breach their duty of loyalty or duty of due diligence, causing the bankruptcy of the debtor. However, the scope of liability is not clearly defined. Moreover, such directors, supervisors and senior managers are not allowed to serve as directors, supervisors or senior managers in any other company within three years after the bankruptcy proceedings of the debtor are concluded.

The legal representative of the debtor or other directly responsible person would be liable if they intentionally cause the debtor to engage in void or voidable actions or do so with gross negligence, causing harm to the interests of the creditor. In this case, the administrator may pursue their liabilities on behalf of the debtor.

The legal representative and, upon the court's decision, financial officers and managers are not allowed to leave their domicile from the time the court's acceptance of the bankruptcy application is served upon the debtor until the bankruptcy proceedings are concluded. In the case of breach, the court may impose an admonition or detention and may impose a fine.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

The EBL is silent as to under what circumstances a parent or affiliate corporation shall be responsible for the liabilities of subsidiaries or affiliates in bankruptcy scenario. However, under the EBL, after the court accepts the bankruptcy application, the shareholders of the debtor should pay off all the unpaid subscribed capital contribution, no matter whether it is due or not.

The concept of 'piercing the corporate veil' is incorporated into the Company Law of the PRC, under which the shareholder should be liable if the company or other shareholders suffers any loss as a result of the shareholder's abuses of its shareholder's right; the shareholder shall be jointly liable for the company's debt if the shareholder abuses the independent status of the company and the shareholder's limited liability to escape debt, substantially undermining the creditor's interests. However, in practice usually the court would be highly cautious in holding the shareholder liable.

Under exceptional situations, a court can order to distribute group company assets pro rata without regard to the assets of the individual corporate entities involved. In practice, such orders are issued where group companies lack corporate independence and their personnel, management and assets are highly mingled.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Pursuant to the EBL, certain restrictions would apply to claims by insiders or non-arm's length creditors. Specifically:

- employees' claims for wages rank third in priority in bankruptcy distribution (ie, after costs of bankruptcy proceedings and debts for common benefit are cleared), together with the other employment-related claims. However, directors, supervisors or other senior managers could only be paid under this rank up to the average wages of the debtor's employees. Any wage exceeding the average level would be treated as unsecured claims with lowest priority in the bankruptcy distribution;
- during reorganisation, shareholders of the debtor are not allowed to request distribution of dividend;

- directors, supervisors or other senior managers are not allowed to transfer their equity of the debtor to any third party, unless approved by the court; and
- abnormal incomes and embezzlement by directors, supervisors or other senior managers, which are obtained by taking advantage of their positions, should be reclaimed by the administrator. Under the 2013 Interpretations, 'abnormal incomes' include, among other things, performance-based bonuses and salaries obtained when the debtor is generally in default of wage payments to most employees. The directors, supervisors and other senior managers' claims towards the debtor, which arise after they return the abnormal income, could be treated as unsecured ordinary claims in distribution (but wages within average level are deemed priority claims as the other employment-related claims).

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Under the Property Law of the PRC, the mortgagee and mortgagor may agree on how to dispose the collateral when the debtor is in default. The same is applicable to pledge and lien. However, once the debtor is in bankruptcy proceedings, under the EBL, the administrator should be responsible for managing and disposing of the debtor's assets, including the collateral, subject to the creditors' meeting's approval.

During reorganisation, enforcement of the security interest against the debtor's assets should be stayed. However, if there is risk of damage to the collateral or significant depreciation in the value of the collateral, which would result in serious harm to the creditor's rights, the creditor may apply to the court to continue to enforce its security interest.

In the situation of conciliation, the creditor may enforce its right of security interest once the court approves the conciliation petition.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

The Company Law of the PRC principally governs non-bankruptcy liquidation of PRC corporations, together with the Provisions on Several Issues Concerning the Application of the Company Law of the PRC II by the Supreme People's Court.

Unlike bankruptcy liquidation, non-bankruptcy liquidation ensues when:

- the term of the company has expired or any other cause of dissolution has appeared;
- the shareholders' meeting has resolved to dissolve the company;
- the business licence of the company has been revoked or the company has been ordered to be shut down as a result of administrative penalty; or
- the company is ordered to be dissolved by a court upon the request of the shareholder or shareholders holding 10 per cent or more voting rights of the company where the company's deadlock cannot be resolved by other means but to continue the business would cause serious losses to the shareholder or shareholders.

A liquidation group should be established within 15 days after the cause for dissolution occurs; otherwise, the creditor may request the court to appoint a liquidation group. The liquidation group should notify the creditors within 10 days and make a public announcement within 60 days after its formation. Creditors who have received notice should file their claims within 30 days and those that do not receive notice should file their claims within 45 days after the announcement.

Should the liquidation group find that the company's assets are insufficient to clear the company's debts, the liquidation group should file an application to the court for bankruptcy.

### Update and trends

The Enterprise Bankruptcy Law of the People's Republic of China, the Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the PRC issued on 9 September 2011 and the Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the PRC II issued on 5 September 2013 have remained as the three major pieces of legislation applicable to the insolvencies and reorganisations of all 'enterprise legal persons' in China. The Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the PRC III is still pending and under discussion, which will focus on the issues relating to administrator and bankruptcy fees pursuant to the current draft for comments.

In August 2016, the Supreme People's Court issued a notice

concerning the setting-up of a liquidation and bankruptcy division in intermediate courts in certain cities, including but not limited to municipalities directly under the central government and provincial capital cities. Those intermediate courts that have a liquidation and bankruptcy division shall handle compulsory liquidation and bankruptcy cases of enterprises respectively within their jurisdictions.

On 23 June 2016, the Civil Division II of the Supreme People's Court launched an online system named 'Information Website of National Bankrupt Enterprise Reorganisation Cases', with the purpose of increasing the transparency of bankruptcy cases and of facilitating bankruptcy proceedings by using internet and information technology.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

In liquidation, the administrator should request the court to terminate the bankruptcy proceedings where one of the following circumstances appears:

- the debtor's assets are not sufficient to clear the costs of bankruptcy proceedings;
- the debtor has no asset to be distributed; or
- distribution of the debtor's assets is completed.

In conciliation, the court will be requested to terminate the bankruptcy procedures when the debtor enters into conciliation agreement with all the creditors. If conciliation fails, the court should terminate the proceedings of conciliation and declare bankruptcy of the debtor.

The court should decide whether to conclude the proceedings within 15 days after its receipt of the request. A public announcement should be made if the court decides to conclude the proceedings. The administrator then should deregister the debtor with the original registration authority. The creditor may request for further distribution if more assets are found or recovered within two years after the conclusion. However, no additional distribution will be made if the assets newly found or recovered are not enough to cover the distribution expenses and those assets shall be turned over to the state treasury.

In reorganisation, the court should terminate the reorganisation procedures and declare bankruptcy of the debtor, upon the request by the administrator or other interested party, when one of the circumstances occurs:

- the business operation or financial status of the debtor continues to deteriorate and cannot be turned around;
- the debtor engages in deception, or maliciously decreases its assets, or commits any other act that is obviously disadvantageous to its creditors;
- the act of the debtor makes the administrator unable to perform its duties and functions; or
- the debtor refuses to or is unable to carry out the reorganisation plan.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

An interested party may request a PRC court to recognise and enforce a judgment or verdict made by a foreign court in insolvency proceedings (see question 49).

The EBL does not provide special rules for foreign creditors. Under the Civil Procedures of the PRC, which is applicable in bankruptcy proceedings unless the EBL provides otherwise, foreign parties enjoy the same rights and bear the same obligations in civil cases as the domestic parties.

The PRC is not a signatory to any international treaty specifically on international insolvency or on recognition of foreign judgments, but has entered into bilateral treaties on mutual judicial assistance in civil and commercial matters with quite a few countries including France, Spain and Singapore.

The PRC is not considering adopting the UNCITRAL Model Law on Cross-Border Insolvency.

### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

The concept of 'centre of main interests' is not available under the EBL or the Civil Procedures of the PRC.

### Cross-border cooperation

#### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Under the EBL, a local court, upon request, may recognise and enforce the judgment or verdict made by a foreign court in insolvency proceedings, which involves the debtor's assets located within the territory of the PRC, if upon the court's review in accordance with an existing international treaty or agreement to which the PRC is a party (including those bilateral treaties on judicial assistance) or based on the doctrine of reciprocity, the recognition and enforcement of the judgment or verdict:

- would not violate the basic principles of PRC law;
- would not harm national sovereignty, safety or social public interest; and
- would not harm the legitimate interest and benefit of creditors within the territory of the PRC.

The EBL does not provide for cooperation between domestic and foreign courts or insolvency administrators in cross-border insolvencies and restructurings.

Cases with respect to recognising a judgment or verdict made in foreign insolvency proceedings are rarely found in practice. Two local courts in Guangdong Province, the Foshan Intermediate People's Court and the Guangzhou Intermediate People's Court, recognised two bankruptcy judgments respectively in 2001 and in 2005. The bankruptcy judgment recognised by Foshan Court was issued by an Italian court and the other recognised by Guangzhou Court was rendered in bankruptcy proceedings before a French court.

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**Cross-border insolvency protocols and joint court hearings**

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- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

So far, the PRC has not entered into any cross-border insolvency protocol or arrangement for cross-border bankruptcy cases. No court has held a hearing jointly with foreign courts.

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# Croatia

Pavo Novokmet and Andrej Skljarov

Žurić i Partneri

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The principal piece of legislation that applies to insolvencies and reorganisations is the Bankruptcy Act (Official Gazette of the Republic of Croatia (OG No. 71/15), which came into force on 1 September 2015. The Bankruptcy Act regulates two basic types of insolvency proceedings: pre-bankruptcy proceedings and bankruptcy proceedings. Supplemental legislation that also applies to certain aspects of insolvencies and reorganisations consists of but is not limited to the Act on Financial Operations and Pre-Bankruptcy Settlement (OG No. 108/12 – 71/15), the Civil Procedure Act (OG No. 53/91 – 89/14), the General Administrative Procedure Act (OG No. 47/09), the Enforcement Act (OG No. 112/12 – 55/16), the Act on the Securement of Employees' Claims in Case of Bankruptcy of the Employer (OG No. 86/08 – 82/15), the Companies Act (OG No. 111/93 – 110/15), Civil Obligations Act (OG No. 35/05–78/15).

Bankruptcy proceedings can be initiated if a debtor is either insolvent or over-indebted. A debtor is insolvent if he or she is continuously unable to pay his outstanding monetary obligations. Insolvency is considered to have occurred if the debtor has outstanding and unconditional monetary obligations registered within the registry of the Financial Agency (FINA), a state-governed financial mediation company, which have not been settled for more than 60 days; or if the debtor did not pay three consecutive salaries to employees.

A debtor that is a legal entity shall be considered to be over-indebted if its obligations are greater than its assets.

Furthermore, imminent insolvency of the debtor, as a basis for the initiation of pre-bankruptcy proceedings over the debtor, exists if the competent commercial court determines that the debtor will be unable to fulfil its outstanding monetary obligations upon their maturity. The debtor shall be considered to be imminently insolvent if he or she has one or more unsettled monetary obligations registered within the registry of the FINA, or if the debtor is in default of the obligation to pay salaries to employees for more than 30 days, or if the debtor fails to pay employment-related contributions or taxes for more than 30 days following the day on which salaries should have been paid out.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The commercial court of debtor's registered seat has exclusive jurisdiction in pre-bankruptcy and bankruptcy proceedings. The High Commercial Court of Republic of Croatia decides on appeals filed in first instance proceedings.

Historically, competence of the commercial courts was shared with the FINA and other courts, especially in relation to pre-bankruptcy. However, the Bankruptcy Act concentrates competence in pre-bankruptcy and bankruptcy matters solely with commercial courts, starting with those proceedings initiated in September 2015.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Bankruptcy and pre-bankruptcy proceedings cannot be initiated over the Republic of Croatia, funds that are financed from the state budget, the Croatian Health Insurance Institute, the Croatian Pension Insurance Institute, and local and regional self-government units. The respective proceedings cannot be initiated over legal entities whose main activity is the production of weapons or the provision of services to the military, without the prior consent of the Minister of Defence.

Pre-bankruptcy proceedings cannot be initiated over a financial institution, credit union, investment company, investment fund management company, credit institution, insurance and reinsurance company, leasing company, institution for payments and institution for electronic money.

When the implementation of bankruptcy or pre-bankruptcy proceedings over a certain legal entity is excluded, as described above, the shareholders and the founders of the respective entity are jointly liable for its obligations. However, this provision does not apply to limited companies.

Certain creditors may have rights over certain assets held by the debtor, by virtue of law or by virtue of contract, excluding those assets from insolvency proceedings. Such creditors are obliged to file a notification of their rights in prescribed deadlines for the application of claims in insolvency proceedings.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Except for the special regime of the legal entities mentioned in question 3, in case of the insolvency of government-owned enterprises, no special procedure is to be followed and all the general provisions of the Bankruptcy Act shall be applied.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

The Bankruptcy Act provides for the possibility to institute pre-bankruptcy proceedings over an imminently insolvent debtor, as described in question 1. These proceedings are less formal, more time-effective and more flexible than bankruptcy proceedings. Consequently, with this solution the Bankruptcy Act provides a certain amount of protection for debtors that are considered 'too big to fail', allowing them to restore their liquidity or solvency through an open dialogue with their creditors, without conducting bankruptcy.

There are also specific rules and procedures applicable in case of financial difficulties or bankruptcy of certain institutions. For example, the Credit Institutions Act (OG No. 159/13, 19/15, 102/15) provides for specific procedures to be conducted in cases of financial difficulties of banks, as well as additional rules related to their bankruptcy.

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**Secured lending and credit (immoveables)**


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**6 What principal types of security are taken on immoveable (real) property?**

The most common means of proprietary security over real estate are a pledge (mortgage) or the 'fiduciary ownership' (transfer of the ownership of immoveable property to the creditor who remains the owner until the claim is settled). Both mentioned types of security must be registered with competent land registries. Creditors whose security was registered earlier will have priority in the process of the settlement of their claims out of the value of the real estate, once it is sold in enforcement proceedings.

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**Secured lending and credit (moveables)**


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**7 What principal types of security are taken on moveable (personal) property?**

As is the case with real estate, the right of pledge as well as fiduciary ownership can be constituted on moveables. A pledge can be constituted on every moveable property, in whole or on its ideal part, which has monetary value and can be sold. Similarly to moveable property, a pledge can be constituted on claims if they are suitable for the settlement of the creditor's claim.

Pledge on moveables should be publicly registered in order to produce legal effects on third parties. The FINA is competent to hold the registry for the registration of security rights over moveables.

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**Unsecured credit**


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**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

Unsecured creditors should apply their claims into bankruptcy and expect pro-rata distribution of funds achieved during the course of bankruptcy, based on their repayment rank. After bankruptcy is opened, no formal actions for purpose of collection or obtaining security are allowed outside bankruptcy.

As a general rule, in order to collect their claims, unsecured creditors have to initiate enforcement proceedings according to the provisions of the Enforcement Act. Depending on enforcement title and the object of execution, enforcement proceedings can be initiated before the FINA, a court or a notary public. Normally, these proceedings are not difficult or time-consuming, as the bodies deciding on the creditor's enforcement applications must act in limited time frames prescribed by law. However, should the debtor file an appeal, the procedure could be significantly prolonged. If the creditor does not dispose with an enforceable deed of any kind, the procedure could turn into a litigation, which typically takes three to five years.

A court is authorised to issue a decision granting proprietary security to an unsecured creditor before a final and enforceable judgement is obtained, if certain prerequisites are met. The creditor should obtain at least a non-final judgment or payment order against the debtor, and should show that, without the requested decision, any collection would probably be unsuccessful or severely hindered.

Foreign creditors may initiate enforcement proceedings, and any other legal action aimed at settling or securing their claims, with the same rights as domestic creditors, provided that they have fulfilled the formality of obtaining the Croatian personal identification number, issued by the Tax Administration.

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**Voluntary liquidations**


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**9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?**

Liquidation proceedings are prescribed in the Companies Act. They are started with a shareholders' resolution on liquidation of the company, which is registered with the court registry.

The main purpose of liquidation is termination of the company and the distribution of all of its assets, after all the company's liabilities towards the creditors are settled. The appointed liquidators shall give notice to the company's creditors to file their claims. Such a notice is published three times at intervals of between 15 and 30 days in the company's journals. For most types of companies, creditors should file their

claims with the company within six months of the publication of the last notice. The company must directly inform all of the known creditors.

Assets of the company that remain after fulfilment of all liabilities shall be distributed to the shareholders in proportion to their shares in the company's capital, unless other criteria are established in the corporate documents of the company. If in any given moment, on the basis of the claims filed, the liquidators establish that the company's assets do not suffice to settle all the creditors' claims, they shall immediately suspend the liquidation and propose initiation of bankruptcy proceedings.

After the company's assets have been distributed among the shareholders, the liquidators shall submit to the shareholders' meeting the final liquidation financial statements and the report on the completed liquidation.

The liquidators shall file for the company's deletion from the commercial court register. Upon the deletion, the company ceases to exist.

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**Involuntary liquidations**


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**10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

Involuntary liquidation is not recognised by Croatian law as a separate legal institute.

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**Voluntary reorganisations**


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**11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

Voluntary reorganisation can be achieved through pre-bankruptcy. The debtor can initiate pre-bankruptcy proceedings if he is considered imminently insolvent, as described in question 1. Pre-bankruptcy is always voluntary as it is initiated directly by the debtor or by a creditor with the consent of the debtor.

The application for the opening of pre-bankruptcy proceedings must be accompanied by the debtor's financial statements not older than three months, the description of the debtor's negotiations with the creditors (if any), evidence of the total assets, evidence the total revenue for the previous business year and the number of employees in the previous month, as well as the restructuring plan. The restructuring plan is the basis for the pre-bankruptcy settlement that will be proposed to the creditors in the respective proceedings.

Pre-bankruptcy proceedings produce legal effects as of the day when the court's decision on the opening of the proceedings has been published on the court's online notice board. Some of the essential legal effects of opening pre-bankruptcy proceedings are the following:

- All creditors are obliged to apply their claims within the deadline determined in the decision on the opening of the proceedings.
- The debtor can only make payments related to the ordinary course of business.
- Initiation of litigation, enforcement or administrative proceedings or proceedings aimed at securing claims against the debtor is prohibited, while all ongoing proceedings shall be suspended.
- The FINA suspends the seizure of funds on the debtor's accounts, except with respect to the claims concerning salaries, severance payments and temporary injunctions issued in criminal proceedings.

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**Involuntary reorganisations**


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**12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

Involuntary reorganisation can be achieved in bankruptcy. Bankruptcy proceedings can be initiated by the creditors over a debtor that is insolvent (see question 1), regardless of the debtor's consent, although the debtor can initiate bankruptcy as well. The creditor is obliged to prove probability of his or her claim and probability of debtor's insolvency.

Aside from the creditors and the debtor, the FINA can also initiate bankruptcy. It is obliged to do so if the debtor has unpaid monetary obligations registered within the registry of the FINA for a period exceeding 120 days. Bankruptcy proceedings produce legal effects as of the day when the decision on the opening of the proceedings has been published on the court's online noticeboard.

Some of the essential legal effects of opening of bankruptcy proceedings are the following:

- Authorities previously held by debtor's corporate bodies are transferred to the bankruptcy administrator (as well as the authorities of a natural person to dispose of his assets if the debtor is a natural person).
- Litigation proceedings involving bankruptcy estate are assumed by the bankruptcy administrator on behalf of the debtor.
- Initiation of new enforcement proceedings over the bankruptcy estate is generally prohibited, whereas any ongoing enforcement proceedings shall be suspended.
- The bankruptcy administrator is authorised to choose whether to continue the debtor's existing contracts that have not been completely fulfilled.
- Opening of bankruptcy is a justified reason for termination of debtor's labour agreements.
- Legal actions of the debtor that are taken prior to the opening of bankruptcy proceedings that undermine the satisfaction of the creditors (creditors' damage), or put certain creditors in a favourable position (preferential treatment of creditors), may be contested by the bankruptcy administrator or other creditors.
- Creditors are obliged to submit their claims within the deadline determined at the opening of the proceedings.

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Initiation of bankruptcy is mandatory, if insolvency or over-indebtedness, as defined in question 1, occur. The following persons are obliged to submit a proposal for the opening of bankruptcy:

- an authorised representative of the company under the law, such as a director or a liquidator;
- a member of the supervisory board of the debtor, if the debtor does not have an authorised representative, if that person could have known about the existence of bankruptcy reasons and the lack of authorised representatives of the company; and
- a shareholder of a limited liability company if the company lacks an authorised representative and the supervisory board, if that person could have known about the existence of bankruptcy reasons and the lack of authorised representatives of the company.

Persons listed above are obliged to file for bankruptcy within 21 days after insolvency or over-indebtedness occurs. They are personally liable to creditors for any damage they caused by not submitting a proposal for the opening of bankruptcy proceedings according to the mentioned provision. Management board members and liquidators could also face criminal responsibility; failure to initiate bankruptcy is a felony, with the prescribed penalties of a monetary fine or imprisonment of up to two years.

Any legal actions undertaken during insolvency or over-indebtedness are under increased risk of being subsequently contested by the bankruptcy administrator or creditors.

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

During pre-bankruptcy proceedings, the debtor can only make those payments that are necessary for his or her ordinary course of business, and in relation to supplies made after the opening of pre-bankruptcy. Suppliers of the debtor should respect the arm's length principle. Otherwise, their actions might be annulled as detrimental to other creditors, as explained in question 39.

During bankruptcy, the bankruptcy administrator assumes management of the debtor, as explained in question 12. In the case of pre-

bankruptcy proceedings, directors retain their representation powers; however, they must abide with the aforementioned rule of conducting only those payments that fall within the scope of the ordinary course of business.

The court is authorised to permanently supervise the bankruptcy administrator and the pre-bankruptcy trustee, having the power to revoke them from their position.

In bankruptcy, the court can constitute a committee of creditors for the purpose of assistance to the bankruptcy administrator and supervision of his work. The creditor's assembly, a permanent body of all creditors in the proceedings, has the same authority as the committee of creditors but it also has additional powers of reaching various resolutions with respect to the bankruptcy proceedings.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

As a general rule, both during pre-bankruptcy proceedings and bankruptcy, there is no possibility of initiation of litigation, enforcement, administrative proceedings or proceedings against the debtor that are related to claims that arose prior to the opening of proceedings, whereas all ongoing proceedings shall be suspended.

Creditors with the right of separate settlement (such as pledge holders) generally preserve their right of separate settlement directly from the object of security.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

In pre-bankruptcy proceedings the debtor could obtain secured or unsecured loans only upon consent of the pre-bankruptcy trustee.

In bankruptcy proceedings, the bankruptcy administrator is the authorised representative of the company and as such he could acquire loans, provided that other bodies of the bankruptcy provide their approval. Having in mind the legal nature and the purpose of bankruptcy (settlement of creditors), such loans could be contemplated as a part of a bankruptcy plan, submitted to the creditors for the purpose of continuation of the creditor's business through restructuring. Such loan would be regarded as an expense incurred by the bankruptcy estate, and would have settlement priority in relation to bankruptcy creditors.

During liquidation, the liquidator is only allowed to take legal actions necessary for the closure of the business of the company, collection of receivables, cashing in the remaining assets and paying the creditors. If obtaining a loan could be regarded as a step in fulfilling the above goals, a loan could be obtained.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Liquidation is neutral with regard to set-off.

If the creditor had the right to set-off at the time of the initiation of bankruptcy, he shall be allowed to exercise such right and the initiation of the bankruptcy proceedings shall have no effect on the creditor's right. However, should the claims on which the set-off is based be conditional or not yet due at the moment of initiation of the bankruptcy proceedings, the set-off may be conducted only in the moment when the required conditions are met.

If, during bankruptcy proceedings, the claim to be offset becomes due or unconditional prior to the time that the set-off could be conducted, a set-off shall be excluded. The set-off is explicitly forbidden where the creditor's obligation arose after the opening of bankruptcy proceedings. Also, set-off is excluded if the creditor acquired his or her claim from another creditor after the opening of bankruptcy proceedings, or within the period of six months before the opening of bankruptcy and the creditor knew or should have known that the debtor became insolvent or that pre-bankruptcy or bankruptcy was initiated.

Set-off is also forbidden if the prerequisites for set-off were achieved by a voidable legal action.

With respect to the pre-bankruptcy settlement procedure, previous regulation provided for set-off to be conducted at the time of establishing of the applied claims, while the new regulation contained in the Bankruptcy Act does not explicitly regulate this matter, and a consistent practice regarding set-off in pre-bankruptcy is yet to develop.

### Sale of assets

- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

Each alienation of assets done by the debtor is allowed in pre-bankruptcy proceedings only upon consent of the pre-bankruptcy trustee, while such actions of the debtor in bankruptcy proceedings regularly conducted if creditor's assembly decided not to continue debtor's business or if allowed by the bankruptcy plan, as explained under question 14. Regarding liquidation proceedings, since the purpose of such proceedings is the sale of the assets and the payment of the creditors and shareholders of the liquidated company, sales are naturally allowed.

If assets of the bankruptcy estate are sold as a whole, the purchaser acquires assets as they stand under the provisions of general law. Therefore, if the respective assets are 'free and clear' they shall be acquired in such state. However, if pledges are constituted over respective assets, generally assets will be transferred with such pledges, unless otherwise determined by the respective sale purchase agreement.

Assets are sold 'free and clear' if the sale of an individual asset is made to satisfy a pledge holder, which is typically done through a public auction.

In cases of sale of debtor's assets as a whole, the sale is made according to the rules agreed by the creditors, while applying the provisions of the Enforcement Act. Since the creditors are free to determine the rules of the sale, there is no obstacle to instituting a 'stalking horse' bids system.

According to rules of the Enforcement Act, which apply in the sale of assets in bankruptcy proceedings, creditors are allowed to purchase the assets themselves. Nevertheless, since the rules for set-off of claims shall apply in such scenario, and since the creditor's obligation to pay the price of the assets arose after the opening of the bankruptcy proceedings, set-off shall be forbidden, as explained in question 17. Therefore, the price of the assets will effectively be paid by the creditor who purchased them. Exceptionally, if a creditor holds a first-rank right of separate satisfaction over the assets in question, he or she can make the payment by reducing his or her claim.

### Intellectual property assets in insolvencies

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

No special provisions of the Bankruptcy Act regulate granted IP rights in bankruptcy and pre-bankruptcy proceedings. In bankruptcy, the bankruptcy administrator has the authority to choose which contracts shall be executed and which shall be terminated, as stated in question 12.

### Personal data in insolvencies

- 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

The insolvent company may use the personal information that was initially obtained for purposes and in a manner that is in line with the relevant laws (Personal Data Protection Act, OG No. 103/03 - 130/11), if during restructuring such information is continued to be used for the same purposes. In principle, any transfer of such data to third parties is subject to the prior consent of the persons to which the information relates.

### Rejection and disclaimer of contracts in reorganisations

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

Since in pre-bankruptcy proceedings the debtor continues his or her business operations under the supervision of the pre-bankruptcy trustee and the court, contractual obligations can be rejected or disclaimed only under general provision of the Civil Obligations Act. Therefore, if a debtor breaches a contract in force, he shall be liable pursuant to general rules of Croatian contract law.

In bankruptcy proceedings, the bankruptcy administrator could revoke certain contracts at his or her discretion, as explained in questions 12 and 19. Any breach committed after the opening of pre-bankruptcy or bankruptcy could become the basis for a claim that would represent an expense enjoying settlement priority over the claims filed through the due procedure by creditors.

### Arbitration processes in insolvency cases

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

In pre-bankruptcy proceedings, no restrictions regarding arbitration proceedings are prescribed (ie, such proceedings could be initiated in any time during pre-bankruptcy proceedings and are not listed among those that should be suspended upon opening of pre-bankruptcy).

In bankruptcy proceedings, arbitration proceedings regarding bankruptcy estate shall be assumed by the bankruptcy administrator, as mentioned in question 12. No further restrictions are provided by the Bankruptcy Act, therefore, as in pre-bankruptcy proceedings the parties can agree to solve their disputes through such arbitration proceedings. The Bankruptcy Act explicitly provides for the possibility to initiate arbitration proceedings regarding contested claims during bankruptcy proceedings. However, arbitration is rarely used in insolvency proceedings in Croatia.

### Successful reorganisations

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

The prescribed elements of the restructuring plan in pre-bankruptcy include, among other, all facts regarding the insolvency of the debtor, detailed financial calculations regarding the debtor's liquidity, measures of financial and operational restructuring and their effects, projected future business plans and balance sheets, analysis of all the claims with respective plans on how they shall be settled as well as the costs of the restructuring.

In bankruptcy proceedings, the bankruptcy plan consists of a preliminary and an implementation basis. The preliminary basis consists of a list of measures which were taken before the opening of bankruptcy proceedings or which need to be taken in order to create the base for the realisation of the rights of participants, as well as all other data on the basis and consequences of the bankruptcy proceedings that are important for the decision of creditors about the bankruptcy plan. The implementation basis consists of provisions regarding the way the legal position of the debtor and other participants in the bankruptcy proceedings is going to be changed. Different appendixes may be required depending on the content of the plan regarding the settlement of claims, such as, asset overviews, or the debtor's or creditors' statements.

Both in pre-bankruptcy and bankruptcy proceedings, creditors are classified in groups with respect to their legal status. The Bankruptcy Act explicitly provides that the following creditors must be differentiated:

- creditors with separate satisfaction rights;
- creditors that are not considered creditors of lower priority; and
- creditors of lower priority.

Creditors of lower priority do not constitute a separate group of creditors if their claims are terminated when the plan is accepted (which depends on the content of the plan). Creditors with the same legal status could be classified in different groups based on the criteria of their economic interests. However, such classification must be founded on valid reasons and must be explained. Workers always form a separate group of creditors.

Regardless of the above rules, if the legal effects of the plan would be equal towards all creditors, no special groups shall be formed.

The restructuring plan in pre-bankruptcy is accepted if the value of the claims of creditors who accepted the plan is at least double the amount of the value of the claims of creditors who were against the plan in each creditor group, provided that the majority of all the creditors voted in favour of the plan.

The bankruptcy plan is accepted when the value of the claims of creditors who accepted the plan is at least double the amount of the value of the claims of creditors who were against the plan, provided that at least half the creditors voted in each creditor group.

In principle, the plan should not release non-debtor parties from liability since such action would be against the purpose of reorganisation and restructuring proceedings (ie, financial recovery of the debtor and satisfaction of all the creditors).

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

There are no rules for expedited reorganisations. The Bankruptcy Act provides for the possibility to implement shortened bankruptcy proceedings in cases where the debtor does not have employees and has unpaid monetary obligations registered within the registry of the FINA for an uninterrupted period of 120 days, provided that there is no legal basis for the deletion of the debtor from the court registry. However, this fast-track procedure cannot include the reorganisation of the debtor.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A proposed reorganisation is defeated if a plan of debtor's restructuring is not accepted. This can primarily occur if the majority needed for the acceptance of the plan, as explained in question 23, was never reached.

There are additional rules about termination of the proceedings. For example, the court shall terminate pre-bankruptcy proceedings if creditors show probable cause that the plan reduces their rights to such a degree that they would be in a better position if the plan were not implemented at all. Proceedings can also be terminated if the plan does not produce a probability that the debtor will restore liquidity by the end of the current year and in two subsequent years. The proceedings will be terminated also in the case where the plan is not confirmed in 120 days upon the filing of the request for initiation of pre-bankruptcy proceedings (increased by a supplemental 90 days deadline, if granted by the court), etc.

In bankruptcy, the court shall terminate the proceedings if the bankruptcy estate is not enough to settle the costs of the proceedings or the liabilities that exist with regard to the bankruptcy estate, or if an agreement is reached by the creditors on such a termination, etc. Essentially, upon termination of the proceedings, all legal effects of the proceedings described under questions 11 and 12 shall cease to exist.

Should the debtor fail to perform the plan, creditors whose claims are approved in the plan are authorised to initiate enforcement proceedings against the debtor based on such final plan, and ultimately push the debtor into bankruptcy.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

Delivery of notices and decisions is performed through publishing of the relevant documents on the court's notice board, which is available online.

Typically, two main hearings are held during pre-bankruptcy, the hearing for the examination of claims and the hearing for voting on the restructuring plan. Notices are given to creditors regarding each phase of the proceedings, such as decisions on the opening of pre-bankruptcy proceedings, on accepting or disputing individual claims, on appeals, on the confirmation of the pre-bankruptcy agreement, on the termination of the proceedings, etc.

In bankruptcy proceedings, several hearings are usually held. First, a hearing is held for the statement of the debtor regarding the initiated proceedings. A hearing is held in order to determine whether the conditions for initiation of proceedings are met. The hearing during which the bankruptcy administrator explains his or her report to the creditors is usually held immediately after the hearing during which all of the applied claims are examined. A separate hearing is also held for the purpose of discussion and voting on the bankruptcy plan, if proposed. Notifications regarding all these hearings and their outcomes as well as other material and procedural information are available to creditors on the mentioned court website during the entire bankruptcy procedure.

All of the information regarding administration of the bankruptcy estate is available to creditors through reports and plans published during the course of the proceedings (ie, the pre-bankruptcy restructuring plan, the bankruptcy plan, the report of the bankruptcy administrator). The bankruptcy administrator is obliged to provide quarterly reports on the economic position of the bankruptcy debtor (the court can request additional reports). Importantly, all of these documents are available online.

Regarding the release of liabilities owed by third parties, explanation was given under question 23.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

In pre-bankruptcy proceedings the debtor is authorised to pursue claims regarding his or her assets.

In bankruptcy proceedings, only the bankruptcy administrator is authorised to pursue claims of the bankruptcy estate based on principles explained in questions 12 and 15. Creditors are entitled to initiate certain actions in favour of the bankruptcy estate, as explained in question 39.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Pre-bankruptcy does not envisage any committees or boards of creditors, so creditors only take action individually or as a group (through a general vote).

As for bankruptcy proceedings, the Bankruptcy Act authorises the court to constitute a committee of creditors for the general purpose of protection of the creditors' rights. This committee can also be constituted by the decision of creditors reached on the creditors' assembly, a permanent body of creditors in bankruptcy proceedings.

The selection of the members of the committee of creditors is generally within the discretion of the body that constitutes the committee. However, the Bankruptcy Act prescribes that creditors with highest and lowest value of claims must be represented, as well as a representative of employees, unless employees participate in the bankruptcy with only insignificant claims. Outside experts can be appointed into the committee of creditors, if their expertise is deemed useful for the committee's operation.

The principal authorities of this committee are the assistance to the bankruptcy administrator, but also supervision of his or her work. The committee can review the bankruptcy administrator's reports and the business books of the debtor that were assumed by the bankruptcy administrator, file complaints on the work of the bankruptcy administrator, and give various opinions on the debtor's business when asked by the court.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

The Bankruptcy Act contains special rules regarding bankruptcy proceedings over affiliated companies. The court conducting bankruptcy proceedings over the debtor has an authority to check if bankruptcy proceedings over debtor's affiliated companies have been initiated. If this is the case, the court with the exclusive jurisdiction to continue the proceedings for all affiliated companies shall be the court competent for the company that has a dominant influence over the affiliates. If there is no such company, competence is granted to the court to which the motion for initiation of bankruptcy was submitted first.

The competent court shall summon a hearing where it shall be decided whether joint bankruptcy proceedings can be opened. If proceedings are opened over affiliated companies, in such proceedings there will be only one creditors' assembly and creditors' committee and one bankruptcy estate. In such proceedings all mutual obligations between affiliated companies shall cease to exist.

Under the general rule, foreign court decisions on opening of bankruptcy that relate to companies that have assets in Croatia can be recognised by a Croatian court and granted legal effects in accordance with the laws under which they were issued.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Under the general rule, any court decision of the first instance can be contested by an appeal, unless it is specified otherwise for some particular type of decision. Other than this general authority provided by law, additional permissions are not required. Also, when regulating the procedure regarding appeals against first instance court decisions, the Bankruptcy Act does not require security to be posted in order to proceed with an appeal.

### Claims

#### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Creditors must submit their claims to the FINA in a period of 15 days in pre-bankruptcy, while in bankruptcy proceedings the filing must be made to the bankruptcy administrator in a period of 60 days. The deadline is computed after the expiration of an eight-day period as of the publication on the court's online noticeboard, as explained in questions 11 and 12.

In bankruptcy proceedings, creditors are allowed to transfer their applied claims to a third party. By the virtue of such a transfer, the transferee becomes a bankruptcy creditor in the proceedings, based on a notarised document or a statement given by the transferor before the court. There are no rules regarding transfer of claims during pre-bankruptcy, but they should be allowed under the general rules of civil law.

The pre-bankruptcy trustee (in bankruptcy: the bankruptcy administrator), creditors and the debtor may contest claims filed by other creditors.

If the debtor or the pre-bankruptcy trustee (in bankruptcy: the bankruptcy administrator) contested other creditors' claims, the court shall refer the respective creditors to litigation in order to determine the contested claim. In case another creditor contested other creditors' claims, the court shall refer the creditor who contested the claim to initiate litigation in order to determine the contested claim.

The debtor as well as each creditor has the right of appeal against the decision on the determined and contested claims in both pre-bankruptcy and in bankruptcy. The deadline for filing the appeal is eight days, and is decided upon by the court of second instance.

In both pre-bankruptcy and bankruptcy, claims should contain fixed amounts. The Bankruptcy Act explicitly prescribes that determined claims can consist only of the amount of the principal and the amount of interest accrued on the day of the opening of the pre-bankruptcy proceedings. From that day, the accruing of interest stops by virtue of law.

In bankruptcy proceedings, claims regarding interest accrued after the day of the opening of the proceedings shall be deemed as claims of lower priority as opposed to the claims regarding the principal and interest accrued until the day of opening of the proceedings that are deemed higher priority claims. In bankruptcy proceedings, all undue claims become due on the day of the opening of the proceedings, discounted at the applicable interest rate. Any claim that depends on fulfilment of a condition precedent is claimed as if it were unconditional.

### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The court is not allowed to change the rank of a creditor's claim, neither in bankruptcy nor in pre-bankruptcy proceedings.

### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Expenses of the bankruptcy proceedings and other expenses of the bankruptcy estate have priority of settlement.

Secured creditors' claims are settled directly from the sale of the asset over which they hold a security interest. However, all the costs related to the sale of the asset in question are first reimbursed to the bankruptcy estate.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Pre-bankruptcy proceedings do not affect employment agreements.

Opening of bankruptcy is a legitimate reason to terminate a debtor's employment agreements irrespective of provisions stipulated in the agreements or applicable legislation, with a termination notice period of one month. An employee who considers that the termination was not valid can claim his or her rights according to general provisions of the Labour Act (OG No. 93/14).

Liquidation proceedings should represent a valid cause for regular termination of employment contracts under the Labour Act, since the employer is closing all its business activities.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

In pre-bankruptcy proceedings, the employees have no obligation to apply their claims arising from the employment agreement, but rather, the person who applied for opening of pre-bankruptcy should include data about those claims in the application. All the debtor's payments based on the employment agreements shall be deemed as ordinary course of business, as described in question 14.

In bankruptcy proceedings, employees' claims have a higher priority than all other creditors' claims. Therefore, all other second-rank creditors' claims are settled only if the claims of employees are completely settled. This applies to former employees as well.

The Act on the Securement of Employees' Claims in Bankruptcies constituted the Agency for Securement of Employees' Claims in Case of Employers' Bankruptcy (the Agency) as the public authority competent for settlement of employees' claims in case of bankruptcy proceedings initiated over their employer.

The Agency is obliged to settle gross amounts of employees' claims arising from employment contracts, together with all pension-related claims. Certain limitations regarding the maximum amounts of employees' claims that may be settled, claims that may be reported as well as preconditions for submitting respective request are prescribed. After the Agency settles the claims, they are transferred to the Agency by virtue of law, and it can claim them during the bankruptcy proceedings.

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The Bankruptcy Act does not contain any specific provisions regarding environmental problems and liabilities, which would apply in cases of insolvency. However, the Environment Protection Act (OG 80/13-78/15) contains provisions that prescribe that the costs of reparation of environmental damages at the site held by a bankrupt company can, under certain conditions, be treated as expenses of the bankruptcy estate.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Pre-bankruptcy proceedings do not affect the right of separate satisfaction of secured creditors, creditors with the right of exclusion of assets, employees' claims, temporary injunctions in criminal proceedings and tax proceedings for determination of abuse of rights.

In case of termination of pre-bankruptcy or bankruptcy proceedings, all liabilities of the debtor shall survive and the creditors shall be entitled to pursue their claims under general legal provisions.

Naturally, all the obligations of the debtor that were not written off by the pre-bankruptcy settlement or the bankruptcy plan shall survive insolvency proceedings.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In pre-bankruptcy proceedings, distributions shall be done after the conclusion of a final pre-bankruptcy settlement, in accordance with the executed settlement.

In bankruptcy proceedings, distributions shall be made after the bankruptcy proceedings expenses and other bankruptcy estate expenses have been settled, as stated in question 33. Upon the conclusion of the hearing for the report of the bankruptcy administrator, the bankruptcy assets shall be cashed in and distributed according to the decisions of the creditors' assembly and the creditors' committee. Creditors of the same rank are settled on a pro rata basis.

Distributions in liquidation proceedings are explained in question 9.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The Bankruptcy Act does not contain provisions regarding annulment of transactions during pre-bankruptcy proceedings. Therefore, such transactions could be annulled under general provisions of the Civil Obligations Act, which allow actions aimed at annulling transactions that are detrimental to creditors.

In bankruptcy proceedings legal actions of the debtor that are taken prior to the opening of bankruptcy proceedings that undermine the right to even satisfaction of the creditors (creditors' damage), or actions that put certain creditors in a more favourable position (preferential treatment of creditors), may be contested by the bankruptcy administrator and other creditors by a lawsuit. Any omission of the debtor that caused the debtor to lose a certain right or that caused a claim against the debtor shall be considered as a voidable action as well.

Depending on the type of legal action being contested, the debtor's intentions or relationship with the concerned third party, the Bankruptcy Act prescribes different periods and conditions for challenging respective actions. These periods may last from one month up to 10 years prior to the opening of bankruptcy proceedings. The claim for the annulment of the action is submitted against the person in whose favour the respective action was taken. If the request for annulment is accepted by the court, the respective action loses its effects with respect to the bankruptcy estate and the counterparty must return all benefits that came from such action to the bankruptcy estate.

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

As stated in question 39, suspect periods can range from one month to 10 years. Voidable transactions can be disputed by the bankruptcy administrator and the creditors as well. The Bankruptcy Act expressly prescribes the possibility of annulling a debtor's legal actions whenever bankruptcy is open over the debtor.

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### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

As explained in question 13, corporate officers and directors of most common types of companies in Croatia (limited liability company and joint stock company), although they are not liable for their corporation's obligations, may be liable to the creditors for the damage they

caused by not submitting a proposal for the opening of bankruptcy proceedings. Furthermore, according to the Companies Act, in conducting business the directors and members of the supervisory board must employ the care of a diligent and conscientious businessman.

Directors who violate their duties shall be jointly and severally liable to the company for any resulting damage. In the event of a dispute, they bear the burden of proof as to whether or not they have employed the required standard of care.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

The Bankruptcy Act does not contain provisions regarding such responsibilities of parent or affiliated corporations. According to the Companies Act, if a controlling company causes a controlled company to enter into a transaction or to undertake or refrain from undertaking any act that is disadvantageous for such controlled company, without compensating such disadvantage by the end of the financial year or granting to the controlled company an entitlement to any measures serving as compensation for this, such controlling company shall be liable for any damage incurred by the controlled company.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

The Bankruptcy Act does not contain provisions regarding such restrictions on claims. However, according to the Companies Act, if at a time when the company is in crisis and when prudent businessmen would have increased the company's equity capital, a shareholder instead grants a loan to the company, he can claim repayment of the loan during bankruptcy proceedings only as a lower-ranking creditor in bankruptcy.

Furthermore, when a third party, at a time referred to above, grants a loan to the company and if a shareholder has provided security or assumed a guarantee for repayment of the loan, the third party can only file a claim in bankruptcy proceedings to the extent that he or she has not been satisfied after using the security or guarantee. These provisions apply mutatis mutandis to other legal acts of a shareholder or a third party, which in economic terms correspond to the granting of a loan.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

As mentioned in question 33, creditors with the right of exclusion of certain assets will not be affected with the legal effects of the opening of pre-bankruptcy or bankruptcy proceedings, provided that they notified the court in the prescribed deadline for the application of claims on their right.

Regarding the creditors with secured rights, in bankruptcy proceedings such creditors shall be allowed to enforce their rights within bankruptcy proceedings with appropriate application of the Enforcement Act provisions. However, in pre-bankruptcy proceedings, creditors with secured rights are allowed to initiate enforcement proceedings over the respective assets only if they waive their right to participate in the pre-bankruptcy proceedings as ordinary creditors.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

See question 9.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Regarding liquidation, see question 9.

### Update and trends

The Bankruptcy Act came into force on 1 September 2015, and it introduced certain novelties, especially in relation to pre-bankruptcy, which is now much less debtor-friendly. However, because of the relatively short period of time that the Bankruptcy Act has been in force, there is no established practice that can be remarked on or highlighted.

The Act on the Bankruptcy of Consumers was published on 18 September 2015. This Act contains special provisions regarding bankruptcy proceedings that are to be opened against consumers. The main purpose of the Act, as stated in the introductory part, is to 'exempt a fair consumer from the obligations that remain after his assets have been cashed in and distributed to creditors'. This Act came into force on 1 January 2016, and a coherent practice is still to be developed.

Pre-bankruptcy proceedings are formally concluded by a court decision confirming a pre-bankruptcy settlement. Bankruptcy proceedings are formally concluded by the court decision on the confirmation of the bankruptcy plan followed by the decision on the conclusion of bankruptcy proceedings. Both proceedings, however, could be terminated by court decisions for various reasons, as explained in question 25.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

Croatian commercial courts have exclusive jurisdiction for bankruptcy proceedings over a debtor whose centre of business operation is on the territory of the Republic of Croatia. If bankruptcy proceedings are initiated against the same debtor in Croatia and in another state, bankruptcy administrators in these proceedings shall cooperate and shall be obliged to exchange all legally permitted information that can be of importance for the proceedings.

Foreign creditors in liquidations and reorganisations have the same rights as domestic creditors.

Foreign judgments or orders can be recognised under general provisions of the Act Concerning the Resolution of Conflicts of Laws with the Provisions of Other Countries in Certain Matters (OG No. 53/91, 88/01) and under the provisions of the Bankruptcy Act. The decision of a foreign court on initiation of the bankruptcy proceedings and of the approval of bankruptcy plan may be filed by a foreign bankruptcy administrator or by a creditor of the debtor. The Croatian court shall recognise such decision if it was reached by a foreign body that has international jurisdiction under Croatian law, if the decision is enforceable under foreign law and if the recognition is not against the rules of Croatian public policy.

Croatian bankruptcy law is harmonised with European legal sources and generally follows some of the principles set forth in the UNCITRAL Model Law on Cross-Border Insolvency.

### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

As mentioned in question 47, the centre of business operation of the debtor is the legal standard that should be used to determine exclusive jurisdiction of Croatian courts. The registered seat of the debtor shall be presumed as the centre of business operation. If the debtor has its registered seat or registered subsidiary (or in some cases just assets) on Croatian territory, but the debtor proves that the debtor's centre of

business operation is in a foreign country where bankruptcy proceedings cannot be initiated, the Croatian courts shall have exclusive jurisdiction nevertheless.

Other than the general legal standard of the centre of business operation, no additional tests or criteria are prescribed.

#### Cross-border cooperation

**49** Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Regarding cross-border cooperation, see question 47. If the provisions prescribed by the Bankruptcy Act and other applicable legislation

on the recognition of foreign decisions are met, the courts have no authority to refuse to recognise such decisions or to cooperate with foreign entities.

#### Cross-border insolvency protocols and joint court hearings

**50** In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

We are not familiar with any practice showing that courts have entered into cross-border insolvency or bankruptcy protocols and joint court hearings with courts in other countries.

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# Cyprus

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Bankruptcy Law and the Bankruptcy Rules, as amended, relate to personal insolvency. Further, the Insolvency of Individuals (Personal Repayment and Relief Plans) Law 65(I)/2015 provides additional provisions for handling of insolvent individuals.

The Companies Law, as amended, governs corporate insolvencies and reorganisations. Amendments to the Companies Law passed earlier this year have introduced the notion of examinership into Cyprus law whereby companies may be reorganised in order to meet their financial obligations. Furthermore, the Companies Law allows for corporate reorganisations, which under section 30 of the Income Tax Law 118(I) of 2002, as amended, includes the following: merger, division, partial division, transfer of assets, exchange of shares and transfer of registered office.

Certain provisions of the Bankruptcy Law regarding the rights of secured and unsecured creditors are also applicable to the winding up of insolvent companies.

Section 211(e) of the Companies Law, gives the Cyprus courts the power to issue an order for the winding up of a Cyprus company when the company is deemed 'unable to pay its debts'. According to section 212 of the Companies Law, a company will be deemed 'unable to pay its debts' (and therefore insolvent) if one of the following occurs:

- if the company fails to settle or secure a liquidated debt or obligation in excess of €5,000 within 21 days from receipt of a written demand from a creditor delivered to the registered address of the company requesting that the outstanding amount owed be settled;
- if an order for execution is issued or any other proceeding is taken by a court on any judgment, decree or order in favour of a creditor of the company and that order is returned either fully or partially without being satisfied; or
- if to the satisfaction of the court it can be proven that the company is unable to pay its debts when such debts are due and payable. In determining whether a company is unable to pay its debts, the court shall take into account the contingent and prospective liabilities of the company; or
- if to the satisfaction of the court it can be proven that the value of the assets of the company is less than the amount of its liabilities, taking into account the contingent and prospective liabilities of the company.

A similar test is applied for individuals but with a number of provisions and restrictions with respect to reasonable income allowing for the upkeep of the individual as well as for reasonable minimum assets that will allow him or her to earn income (tools, vehicle etc).

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Insolvency proceedings are handled by the district courts. For personal insolvencies, the district court of the district where the individual is located is the applicable court where the insolvency will be processed. Applications to liquidate (wind up) a company must be submitted to the

district court of the district where the registered office of the company is located.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Under the relevant legislation, there is no exclusion of any entity, corporate or personal, from insolvency proceedings, other than the Central Bank of Cyprus, which is established constitutionally. Special arrangements apply to the resolution of banks and other financial institutions. In corporate proceedings no assets are excluded from claims of creditors other than those that are not beneficially owned by the debtor (ie, property held on trust). In individual insolvencies, a person may apply to the courts in order to request an order for the relief from debts whereby the debts are erased by the court if the individual has a monthly available income of less than €200 (which is calculated on the basis of a formula taking into account all sources of income and other maintenance expenses), assets of less than €1,000 and is a resident of Cyprus. Under the same law, assets do not include chattels that are necessary in order for the individual to maintain a minimum quality of life (books, tools, white goods, vehicles etc). Special provisions for specialised equipment for medical needs also apply.

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Government-owned enterprises, otherwise known as semi-governmental organisations (such as the Cyprus Telecommunications Authority, the Cyprus Electricity Authority, the Ports Authority, etc), are incorporated based on a separate law that is enacted for each such organisation. Normally there are no provisions in the law regarding the dissolution and liquidation of such organisations. In the event that the enterprise must for whatever reason be liquidated, the specific law relating to such an enterprise is amended and special provisions for liquidation and dissolution are introduced therein.

An example of a semi-governmental body that has been dissolved is the State Fairs. This was dissolved on the basis of an amendment to the State Fairs Authority Law, which resulted in the transfer of all moveable and immovable property owned by the Authority, and any rights or obligations of the Authority relating to such property, to the government.

## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Cyprus had implemented the Resolution of Credit and Other Institutions Law 17(I)/2013 (the Resolution Law) that allowed the Resolution Authority of Cyprus, comprising the Central Bank of Cyprus, to take steps in order to maintain stability in the banking and financial services industry and that granted the power to the Resolution Authority to adopt and implement resolution measures regarding

affected institutions. The Resolution Law was implemented ahead of the EU Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 (as amended) (BRRD) because of the difficulties faced by Cypriot banks in 2013. The Resolution Law was replaced by legislation enacted on 18 March 2016, Law No. 22(I)/2016 on the Regulation of the Resolution of Credit Institutions and Investment Companies and related matters for the purposes of harmonising the measures available under Cyprus law with those set out in the BRRD.

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### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

Mortgages allow the beneficiary thereof to, inter alia, sell, repossess the property or to start a foreclosure procedure. A mortgage constitutes a contractual right for the benefit of the mortgagee and constitutes a charge on the property. Mortgages under Cyprus law can either be legal or equitable. A legal mortgage is the common type of security granted over immoveable property in Cyprus and it gives a legal right in the property. It must be registered at the Land Registry of the district where the immoveable property is located. If such mortgage is given by a Cyprus company, it must also be registered with the Department of the Official Receiver and Registrar of Companies (ROC). An equitable mortgage grants equitable rights to the lender rather than a legal right.

Following an interested party's application the court may issue an order for the registration of a memorandum on real estate, filed at the Land Registry Office.

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### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

In Cyprus, moveable property is considered to be any property not falling within the definition of immoveable property. It therefore includes shares, securities, financial instruments, cash, goods, equipment, trading stock, works of art, aircraft and ships.

The most common type of security taken over shares is a pledge, which sometimes includes a fixed charge. A pledge can also be taken on bank accounts. A pledge of shares held by a Cyprus company (pledgor) in a foreign company is registrable against the pledgor as a charge under section 90 of the Companies Law with the ROC, in order to be valid against the pledgor's liquidator; a pledge of shares held by a Cyprus company in another Cyprus company, as well as an assignment of rights emanating from shares or any other charge over share certificates, shares or rights emanating from shares is exempted from such registration.

A lien, whether a common law legal lien or an equitable lien, can also be taken on moveable property, usually goods, that are being transported. The lien gives the holder the right only to retain the debtor's property until payment and does not include a right of sale. Therefore, a carrier's lien, that is to say his or her right to retain possession of the goods, is extinguished against payment of transport costs.

Retention of title (or *Romalpa* clauses – after the English case of *Aluminium Industrie Vaassen BV v Romalpa Aluminium Limited*) is also used, providing that the title to the goods remains vested in the seller until certain obligations, usually payment of the purchase price, are fulfilled by the buyer.

Goods, equipment and company assets are most commonly secured by a floating charge, that is to say a security interest that 'floats' until an event of default occurs or until the company goes into insolvent liquidation, at which time the floating charge is said to 'crystallise' and attaches to all the relevant assets. The floating charge has the advantage of allowing the debtor to deal with the assets in the ordinary course of business. In practice floating charges are created over the whole business and undertaking of a company, present and future.

Ship mortgages over Cyprus-registered vessels are used extensively in ship finance transactions. The same are registrable with the Registrar of Cyprus ships or at the Cyprus consulate overseas; if the mortgaged vessel is owned by a Cyprus company, the mortgage must also be registered with the ROC.

Where the Financial Collateral Law 43(I)/2004 (FCAL) and EU Directive 2002/47/EC (FCD) are applicable, perfection requirements such as registrations with the ROC or special requirements of witnessing of documents (eg, pledges) under the Contract Law, do not need to

be satisfied; further, there are no restrictions on enforcing security in insolvency situations: for instance, where a company is in the process of being wound up, the collateral taker retains the right to deal with its security, including a fixed or floating charge, upon crystallisation, for its own purposes.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Any creditor (whether local or foreign) can bring actions against individuals and companies at the place of residence or registered office respectively in order to recover debt. If the creditor has reasons to believe that the debtor may dispose of assets in order to avoid debt recovery, an injunction may be sought from the district court in order to freeze assets. No other pre-judgment procedures exist. Once the creditor has obtained a judgment against the debtor, a number of enforcement tools exist in order for the creditor to recover the debt. Some examples include writ of execution for the sale of moveables, charges over immoveable property, orders for the delivery or possession of goods and bankruptcy proceedings, garnishee proceedings, writ of delivery of goods, possession of land and writ of sequestration.

It should be noted that during an examinership procedure unsecured creditors are prohibited from bringing an action.

Where the claim of the unsecured creditor is substantiated, such creditor may initiate the procedure for the winding up of the company (see question 10).

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

The shareholders of a company express their wish to liquidate the company by written instructions to the board of directors. The directors proceed to pass a resolution to discontinue the company's activities, to close its bank accounts and to instruct the auditors to prepare financial statements. The auditors perform their audit and provide the board with an up-to-date balance sheet. The final tax return of the company is then submitted to the tax authorities. The next step is for the board to make a full enquiry into the affairs of the company with a view to forming the opinion that the company will be able to pay its debts in full, within a period not exceeding 12 months from the commencement of the winding up and prepare a declaration of solvency. An extraordinary general meeting is convened and held where the shareholders appoint a liquidator to act for the purposes of the winding up. The appointed liquidator must be licensed as an insolvency practitioner and must meet the criteria set out in the recently enacted Insolvency Practitioners Law 64(I) of 2015 (the Insolvency Law) (specifically section 14) and the Insolvency Practitioners Regulations of 2015.

The company must be able to meet its debts in order to enter into a voluntary liquidation. If, during the liquidation process, the company is found to be insolvent, the creditors may appoint an alternate liquidator in which case the liquidation will be converted to a creditors' liquidation.

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Any creditor may apply to the district court where the debtor is located in order to apply for the liquidation of the debtor. In order to successfully place the debtor in liquidation, the creditor must prove to the court that the debtor is unable to pay his or her debts (section 211(e), the Companies Law) as per the insolvency test set out in question 1.

In addition to this, a creditor may also apply for the liquidation of the debtor if the execution or other process issued on a judgment against the company in favour of a creditor of the company is returned unsatisfied. Another option is to prove to the satisfaction of the court that the value of the assets of the company is less than the amount of its liabilities, taking into account the contingent and prospective liabilities of the company.

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## Voluntary reorganisations

### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The latest amendment of the Companies Law, passed into law in mid-2015, introduced the concept of examinership in Cyprus law. Examinership is a process providing for the financial reorganisation of a viable company with liquidity problems and that aims to keep the business alive and pay back creditors over time. It also seeks to provide relief from actions of creditors of the company so that the company has the time to reorganise its financial affairs.

The court may appoint an examiner (an individual who fulfils the criteria of insolvency practitioners) in the event that the company fulfils the following criteria (section 202A(1)):

- the company is open to claims or will be unable to service its debts;
- no liquidation against the company has been approved and published in the Official Gazette of the Republic of Cyprus; and
- no court order has been issued for the liquidation of the company;

The court will only issue an order for examinership if the company is found to be a 'going concern' (section 202A(3)) and has a reasonable prospect of survival. This is determined by a report that is prepared by an independent adviser (who is either the auditor of the company or a person who has the qualifications to act as an auditor), which is attached to the application for examinership and must provide basis to the court that there are reasonable prospects of survival (as defined in section 202B (3) and (4)).

Applications for examinership may be made by the following interested parties (section 202B):

- the company itself;
- any creditor or future creditor, including a company employee;
- members of the company who, at the time of the application, hold no less than 10 per cent of the paid up capital of the company that has voting rights attached to it;
- a guarantor of the company; and
- any entity as listed above, jointly or severally.

With the submission of an application for the appointment of an examiner the company is under court protection for a period of four months. During this period a receiver cannot be appointed and the company cannot be placed under liquidation (section 202H). In addition, no actions can be made against assets of the company without the consent of the examiner (this includes mortgages, confiscations and lease agreements).

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## Involuntary reorganisations

### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

The examinership scheme, as described above in question 11, allows for the procedure to be commenced by either the company or members of the company (voluntary) or by creditors or guarantors (involuntary) or by a mixture of all the above-mentioned interested parties. The process remains the same in all eventualities and therefore there are no alternate effects other than those described above in question 11.

Apart from financial reorganisations as above, a creditor of the company may initiate the procedure for the reorganisation of a company by making an application in a summary way requesting a meeting of the creditors. If the court orders the convening of such meeting and if a majority in numbers representing three-fourths in value of the creditors agree to any compromise or arrangement, the compromise or arrangement shall, if sanctioned by the court, be binding on all the creditors or the class of creditors, or on the members or class of members, as the case may be, and also on the company or, in the case of a company in the course of being wound up, on the liquidator and contributors of the company. The compromise or arrangement includes merger, division, partial division, transfer of assets, exchange of shares and transfer of registered office.

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## Mandatory commencement of insolvency proceedings

### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

In order for a company itself to be able to commence liquidation proceedings, it must be able to satisfy all creditors (current and expected). Therefore, the directors of the company must declare that the company is solvent for the purposes of the voluntary liquidation. Any director making a declaration of solvency for such purposes without having reasonable grounds for making such a statement, commits an offence and on conviction is liable to imprisonment or to a fine or to both. If the liquidator who is appointed within the course of a voluntary liquidation is of the opinion that the company will not be able to meet its obligations and pay all debts, he or she must call a meeting of creditors and supply them with all information regarding the company's financial position and affairs. From that meeting onwards, the voluntary liquidation is converted to a creditors' liquidation.

Where the company continues trading while being insolvent, the directors face the risk of incurring personal liability charges for fraudulent trading (see question 41), however, such claims are rare in Cyprus.

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## Doing business in reorganisations

### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

The examiner, during the period of examinership, has the following powers that are prescribed in section 202IB:

- to convene, set the agenda and preside over a director and shareholder meeting;
- to cancel or correct any action or omission, behaviour, decision or contract against the company; and
- to notify any third person that has contracted with the company that a provision of their contract is not binding to the company in the event that this provision affects the survival of the company in a negative manner.

In general, section 202(1) provides that no payment may be made by the company during protection period for the satisfaction or settlement either wholly or in part of any obligation that was created against the company prior to the filing of the examinership petition unless the report of the independent expert includes a recommendation that all or part of such an obligation is settled or satisfied or if the examiner authorises such a payment.

The court may, following an application by the examiner or any other interested party authorise the payment or settlement of an obligation, either partly or in full if it is satisfied that omitting such payment or settlement substantially reduces the prospects of survival of the company or any part of its business as a going concern.

Subsection 3 further specifies that utility service providers, including those who provide electricity, telephony services, water and internet services, continue the provision of their services to the company provided they are paid for any expenses that are incurred during the protection period.

The company during the examinership period continues business as usual, under the restrictions and provisions contained in the law that will allow the examiner to assess and reorganise the financials of the company.

The examiner has the following powers in relation to secured assets (as per section 202IST):

- the general right to handle and dispose of secured assets after applying to the court for a such permission;
- in the event of sale of assets covered by a floating charge, the possessor of the charge has the same priority given under the floating charge;

- in the event of sale of assets covered by a fixed charge, the possessor of the charge will be paid the whole amount that corresponds to the secured assets from the net proceeds of the sale; and
- in the event that the net proceeds are less than the market value of the asset, the court may decide the amount that must be added to the net proceeds in order to repay the possessor of the fixed charge.

The officers of the company are required to assist and aid the examiner in his role (section 202IG). In addition, the court may order that the examiner assumes the powers and duties of the directors of the company (section 202ID). The court, before making such order, will take into account whether the affairs of the company are conducted in such a manner that may possibly affect the wellbeing of the company, its employee or its creditors as a class. Also, it will take into account whether it is advisable, in order to preserve assets or to safeguard the interests of the interested parties, that the exercise of powers by the board of directors or the management of the company is curtailed or regulated.

After insolvency proceedings are commenced and a liquidator is appointed, unlike examinership, the directors no longer have any powers to manage the company and its business.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

When a winding-up order has been made or a provisional liquidator has been appointed, no action or proceeding shall be proceeded with or commenced against the company except by leave of the court and subject to such terms as the court may impose.

At any time after the presentation of a winding-up petition, and before a winding-up order has been made, the company, or any creditor or contributory:

- where any action or proceeding against the company is pending in any court, may apply to the court for a stay of proceedings; and
- where any other action or proceeding is pending against the company, may apply to the court to restrain further proceedings in the action or proceeding.

If the company is undergoing examinership proceedings, no claims can be brought or orders made against the company.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Under the Bankruptcy Law, a bankrupt individual may not obtain credit €650 or more, or enter into trade, without disclosing that he or she is bankrupt. Such debts will rank after all other debts and shall not have priority over existing debt. If he or she does so, including entering into trade on the basis of a name other than that under which he or she was declared bankrupt, then such person is guilty of a crime and is imprisonable for a period of up to three years.

Insolvent companies cannot enter into further transactions after a liquidation order (unless they exit liquidation following an arrangement with their creditors), the liquidator, as per section 233, is entitled to raise money on the security of the assets.

Under examinership rules, further credit may be obtained if it is important for the success of the examinership. The examiner has the ability to certify certain new expenses as 'expenses which have been duly incurred'. This includes obtaining further credit to the company as a provision for new credit facilities is contained in the law (necessary and duly obtained further expenses). Creditors who have granted such facilities to the company are to be repaid before all other creditors (except creditors who have fixed charges). In addition, it is worth mentioning that utilities (such as water, electricity and telecommunication services) are obliged to continue providing services to the company during the protection period, given that the expenses made during the protection period will be considered 'necessary expenses'.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Set-off is available to creditors, subject to provisions contained in the Companies Law. In addition, the court may, at any time after making a winding-up order, make an order against any contributory to pay more money due from him to the company.

The Bankruptcy Law (which is also applicable with respect to the liquidation of insolvent companies) provides that in the case of mutual debts, mutual claims and mutual transactions existing between a creditor and the debtor then an account is taken of all the claims on either side and they are set off against each other and the difference is payable by the net debtor to the net creditor. The only exception is in the case of debts created by the debtor after the insolvency proceedings were initiated where the creditor was aware of the existence of such proceedings at the time of the creation of the debt.

Set-off or netting is further allowed on the basis of the FCAL, which provides that on the occurrence of an enforcement event, the collateral taker shall be able to realise any financial collateral provided under and subject to the terms agreed in a security financial collateral arrangement. It further provides that if an enforcement event occurs while any obligation of the collateral taker to transfer equivalent collateral under a title transfer financial collateral arrangement remains outstanding, the obligation may be the subject of a close-out netting provision and that a close-out netting provision can take effect in accordance with its terms notwithstanding the commencement or continuation of winding-up proceedings or reorganisation measures in respect of the collateral provider or the collateral taker. Netting provisions are additionally protected under Directive 2001/24/EC on the reorganisation and winding up of institutions and the respective national Business of Credit Institutions Laws and Co-operative Societies Law 22/1985.

Although the right of set-off is recognised and protected by both the BRRD and the Resolution Measures Law an enforcement event within the meaning of the FCAL and Directive 2002/47/EC (which consequentially may trigger the exercise of set-off rights) may not be triggered solely on the basis of the implementation of a crisis prevention measure or a crisis management measure provided that the substantive obligations under the contract, including payment and delivery obligations and the provision of collateral, continue to be performed. Nevertheless provisions are included in both the BRRD and the Resolution Measures Law for the protection of set-off agreements, title transfer financial collateral arrangements, etc.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

When a company has entered liquidation, the liquidator, having assumed control of the company, is entitled to sell any of the company's assets in the way he or she considers most advantageous (ie, auction, private contract). The liquidator may sell assets that are not used as security for creditors (floating charged assets can be sold with the consent of the chargor). The transfer of undertakings as a whole imposes restrictions on the transfer of employees. There are no specific provisions that restrict the use of 'stalking horse' bids as the sale process is at the discretion of the liquidator or examiner (under general duties towards creditors and other interested parties). Credit bidding is permitted as no restrictions exist under the law, again this is at the liquidator's or examiner's discretion.

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

As Cyprus law is silent on this issue one has to look at the licence agreement between IP licensor and the debtor or licensee. The licence agreement may contain a provision giving the right to the licensor to terminate the licensee's right to use it; or the licence may contain a provision to the effect that the IP right is terminated automatically upon insolvency. Neither the Bankruptcy Law nor the Intellectual Property Rights Law give any guidance.

A company's liquidator will be able to continue to use IP rights for the benefit of the winding up, unless the licence agreement provides for instance that the right is automatically terminated when insolvency proceedings commence.

The ability of the insolvency representative to terminate the debtor's agreement with a licensor or owner and nevertheless continue to use the IP for the benefit of the estate seems illogical.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Companies Law and the Insolvency Regulations are silent on this issue. Personal information and customer data collected by an insolvent company may be considered as part of its business goodwill and therefore an asset. However, personal information may only be handled and transferred in accordance with the Processing Of Personal Data (Protection Of Individuals) Law 138(I) 2001 (as amended) and relevant EU Regulations and Directives, and under the instructions of the Data Protection Commissioner, as this may be applicable to the type and nature of personal data collected by the insolvent company.

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### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

The Companies Law contains adequate provisions that enable the court to make any order to amend contracts in order to facilitate the process of reorganisation. The examiner has a wide range of power to amend existing contracts. The consequences of a debtor breaching a contract after the insolvency case is opened depend on the terms of the contract; any claims under such contracts would be ranked as unsecured.

A liquidator is allowed to disclaim onerous property, including contracts. In such case where any part of the property of a company which is being wound up consists of immovable property burdened with onerous covenants, of unprofitable contracts, by reason of its binding the possessor thereof to the performance of any onerous act, the liquidator of the company may with the leave of the court and within the course of a specific period, disclaim onerous property.

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### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

An insolvency process is itself a public process that affects the rights of several third parties that have contractual relations with the company or individual. Therefore, these rights cannot be enforced through

an arbitration process that requires consent and is usually private. In addition, under the Companies Law, the courts have jurisdiction over corporate and individual insolvencies, and only the courts may order liquidations. In the event of a shareholder dispute that leads to an application for liquidation before a court, it may be possible to resort to arbitration if all parties consent, prior to the court ordering the liquidation of the company. In these cases, shareholders' disputes may be arbitrated but failing this, a liquidation order will not be issued by the arbitration tribunal or body.

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### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

The court, as per section 202KE, needs to approve the financial reorganisation plan and decide whether it will approve the proposals for a debt repayment plan. The court must take into account whether the proposals are just and equitable (under principles of equity) under the following principles set out in the law:

- the resuming of normal business activities;
- avoiding employee redundancies; and
- safeguarding creditors so that they are not in a worse position than they would be if the company were to commence liquidation proceedings.

Creditors are classed as secured and unsecured creditors under the plan prepared by the examiner. Officers of the company cannot be released from their liability against the company in the event that fraudulent transactions had been made in relation to preferential treatment of creditors before the examinership period.

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### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

There is no method by which the financial reorganisation is expedited or prepackaged as the process under examinership is relatively brief. It aims to bring a company back to sustainability within a short period of time, with each case examined on its own merits. Depending on the complexity of the financial reorganisation, the time taken for the negotiation process with creditors may vary.

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### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

If the proposal does not meet the criteria described above in question 2 it will be most likely be rejected by the court. In this case, the company will exit the examinership court protection phase (as per section 202KQ) and will be open for claims to its liquidation. Upon confirmation of the reorganisation plan by the court, the proposals become legally binding on all shareholders, creditors and other interested parties (section 202KE). The proposals must be applied and effected, the latest, within 30 days from the court confirmation (section 202KE(10)). Upon activation of the reorganisation plan, the company ceases to be under court protection and the appointment of the examiner is terminated (section 202KQ).

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### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

When a liquidator is appointed in a company, a copy of the order appointing them is delivered within three business days to the ROC, which registers it and publishes the appointment on its official website (section 219 (1)). The creditors of the company are allowed to form a committee and select the liquidator they wish to represent them in

their claims against the company (section 228A). Creditors and contributors of a company may form separate committees in order to select a liquidator. The law provides for the eventuality that these committees do not agree and provides that a third person may be appointed or two persons jointly.

The initial liquidator appointed is the official receiver of Cyprus. Following this appointment, which is made for an interim period, the creditors will then meet to appoint a liquidator of their choice. For purposes of convenience, the official receiver may also suggest a liquidator who will be appointed by the court in the place of the official receiver. The liquidator of the company will publish in newspapers and the official gazette the fact that he has been appointed and will invite all creditors of the company to submit their claims to him.

The liquidator is required under the law to publish all relevant facts of the company and to maintain records books, financial statements and minute books in which he or she is responsible for the filings (section 235). Under section 237, the liquidator is also required to provide information to the official receiver when requested to do so and at least twice annually for as long as he or she is appointed as liquidator. Audited accounts are to be sent to the creditors and contributors of the company by post (section 237(5)). The official receiver also has a wide range of powers available to him that enable the request of information (including the provision of books or accounts) at any time and for any question to be made to the liquidator of a company (section 238).

According to section 240, the creditors who may have formed a committee to appoint the liquidator have the authority and powers to aid the liquidator in his role as well as supervise his functions. Such committees have the power to initiate claims for the company against third parties along with the liquidator.

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#### Enforcement of estate's rights

##### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

As discussed above, the liquidator will take the role of the company and will be able to pursue all claims on behalf of the company. The creditors may pursue the estate's remedies, although in normal circumstances the claim would be pursued at the expense of the company. It is for the liquidator and the creditors to decide whether it is worth pursuing a claim and how this will be best handled. Assignment of a cause of action to one of the creditors may occur if the rights of other creditors are not violated; alternatively, the cause of action may be assigned to the creditors as a class, in both instances the claim will still be pursued in the name of the company. The company will not be liquidated until the remedies from the claim have been received. There is a variety of case law on this matter under Cyprus and English law; although it has not yet been clarified whether assignment to a third party of a bare cause of action (non-tortuous) that is being promoted before the courts by a company placed under liquidation is permissible or not. Drawing guidance from English judgments, such assignments are contrary to public policy and will not be enforced.

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#### Creditor representation

##### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Committees can be formed by the creditors and the contributors of the company separately. Their powers and duties are further discussed above in question 26. Such committees are formed and organised by each class separately and choose representatives to protect their interests.

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#### Insolvency of corporate groups

##### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Each company is considered a separate legal entity and as such each company is subject to separate procedures. Cyprus law does not provide for this, either administratively or for the purposes of aggregation of assets and liabilities.

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#### Appeals

##### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Any court judgment issued in the process of an insolvency proceeding may be appealed at the Supreme Court of Cyprus (in its Appellate function) or by requesting that the judgment be set aside at the district court level, or both. There is no requirement to obtain permission or post security in order to appeal or set aside a judgment.

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#### Claims

##### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Creditors who wish to have their debts processed must deliver proof of their debt to the administrator of the company (in the case that a liquidator, receiver or examiner has not been appointed yet, they will need to apply to the office of the official receiver) within a period of 35 days from the date of the publication, which may be extended. Their proof must be verified, in the form of a court sworn affidavit, and attaching a detailed statement of accounts and vouchers to verify the claim. All proofs will be open to other creditors who have submitted claims. The administrator will have the right to redeem the security of the secured creditor or has the option to apply to the court in order to realise the property comprising the security.

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#### Modifying creditors' rights

##### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

As explained in question 39, the court may invalidate a charge granted by a company and remove the status of secured creditor. This can be made under a number of provisions set out in the Companies Law.

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#### Priority claims

##### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

In the case of winding up or liquidation of a company, claims will rank in priority over any other unsecured claims save for preferential debts, which are mandatorily preferred by law and the order for the distribution of the assets will be as follows:

- the costs of winding up, including disbursements and the fees of the liquidator and any other appointed persons;
- the preferential debts as the same are outlined in section 300 of the Companies Law (local and government taxes due within the 12 months before the insolvency, any unpaid wages and social security contributions for the employees and any unpaid compensation for personal injury during working hours);
- the amounts secured by a floating charge;

- the unsecured ordinary creditors;
- the deferred debts (for example, sums due to the members of the company such as dividends declared but not paid); and
- any surplus will be distributed among the members of the company.

Secured creditors are payable out of the proceeds of sale of the assets subject to the charge. If the charge is a floating charge, the charge holder ranks behind the preferential debts as shown above. If there is a surplus from the sale of the assets subject to the charge, such surplus becomes part of the general pool of assets. If there is a shortfall, the creditor concerned will have an unsecured claim for the shortfall.

#### Employment-related liabilities in restructurings

##### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

During a financial restructuring of a company, the examiner must safeguard as many employee positions as possible, which will, however, enable the company to have a sustainable future. The contractual and legal duties of the company towards the employees in relation to remuneration as well as compensation in the event of dismissal will apply.

#### Pension claims

##### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

It is common that pension fund arrangements in Cyprus are made through provident funds whereas the employee and the employer will have defined contributions for the duration of the employment. Unpaid contributions to the employees' provident fund by the company will rank as a preferential claim.

#### Environmental problems and liabilities

##### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The liquidator of a company will be responsible for handling all matters relating to the company as he or she will effectively take over the management of the company. Therefore, any environmental obligations will be dealt with as they arise. Under section 304, the liquidator is permitted (with the court's approval) to dispose of any onerous property. Although we are not aware of any reported cases that deal with environmental liabilities, we can assume that if there is an environmental concern, the court is likely to issue an order for the control of the environmental problem that will be binding on the company.

#### Liabilities that survive insolvency proceedings

##### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Under liquidation, no liabilities of the debtor will survive, as the company will eventually be dissolved. In an examinership, the company, if the examinership is successful, will be able to continue business as normal, and therefore liabilities will continue to exist. In the case of transfer of undertakings, employee rights will be transferred.

#### Distributions

##### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Distributions are made to creditors after the liquidator and examiner have processed all claims and have valued and sold, reorganised or realised all assets of the company, including any possible set offs and nettings that are applicable. Creditors will then receive compensation from the company, according to the priority of claims and according to the percentage that each creditor will receive given the capabilities of the company to make such payments.

#### Update and trends

The Cyprus Insolvency regime underwent a full revamp in 2015 as several new concepts were introduced, including that of bankruptcy protection under examinership and personal insolvency protection. In addition, the Bank and Credit Institution legal framework, although already utilised, has been updated to conform with the EU bank resolution framework. We are now assessing the effects as the newly introduced provisions and concepts are being put into practice.

#### Transactions that may be annulled

##### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

Any transaction made by the company (a wide-ranging concept that includes payments, deliveries of goods, mortgages and conveyancing, as well as executions or other acts relating to property made or done by or against a company within six months before the commencement of its winding up may be considered to be a fraudulent preference against its creditors and invalid. On the question of fraudulent preference, the court will look into the intentions behind the transaction. The onus is on those who claim to avoid the transaction to establish what the debtor actually intended and that the actual intention was to make a preference among creditors. Floating charges are also valid up to the extent of any cash paid to the company at the time of the creation of the charge unless it is proven that the charge was made while the company was solvent. The liquidation test described in detail above (excess of assets over liabilities and ability to pay debts as they fall due) will apply in the same manner.

#### Proceedings to annul transactions

##### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

See question 39.

#### Directors and officers

##### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The general provisions of fraudulent trading allow for the court to pursue directors personally, in order to pay creditors who have been defrauded because of the directors' misconduct. It should be noted that this claim has a high standard of proof. In addition to the above, directors may be personally liable under several other legislations mainly involving the tax obligations of the company.

#### Groups of companies

##### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Every company is considered to be a separate legal entity, despite corporate group arrangements. Parent companies and associated companies cannot be liable for other companies of the same group except in the event where guarantee agreements have been entered into and given as security for their liabilities. The provisions of fraudulent trading, as per section 311, allow for the court to pursue directors personally, in order to pay creditors who have been defrauded because of the directors' misconduct.

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**Insider claims**
**43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

Non-arm's length creditors will rank *pari passu* with other unsecured creditors. There is no rule that will restrict them in their claim, unless they fall under preferential treatment of creditors or fraudulent transactions as explained in questions 39 and 40 respectively.

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**Creditors' enforcement**
**44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

Assets may be seized with out-of-court pledge enforcement, where the company is obliged to deliver the pledged assets to the pledgor in the event of default. An alternate process whereby assets of a company may be seized out-of-court is when a receiver is appointed in a company under a contractual obligation, in order to seize assets and then resign once these assets have been sold for the benefit of the other party. Following receivership, a company may continue its business operation.

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**Corporate procedures**
**45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

Aside from the liquidation proceedings that require court involvement, where the ROC has reasonable cause to believe that a company is not carrying on business or is in operation or where the directors of the company fall below the minimum number stipulated in the company's articles of association or where the company fails to file any document as required pursuant to the Companies Law, it may commence the procedure for the strike-off of the company, which following the relevant notifications and publications results in the striking of the company off the registry. This procedure may also be initiated by the shareholders, the directors or other officers.

The company can within a period of 20 years from the date of dissolution be restored following a court application by an interested party and the liability, if any, of every director, managing officer and member of the company shall continue and may be enforced as if the company had not been dissolved.

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**Conclusion of case**
**46 How are liquidation and reorganisation cases formally concluded?**

In the case of a members' voluntary liquidation, as soon as the affairs of the company are fully wound up, the liquidator will draw up an account of the winding up showing how it has been conducted and the manner in which the property of the company has been disposed of, and

will call a general meeting of the company to explain this. This meeting is called via an advertisement in the gazette, published at least one month before the meeting. Within one week after the meeting, the liquidator sends to the ROC a copy of the account, and shall make a return of the meeting and its date. The ROC on receiving the account and the return, will proceed with registering the same and at the expiration of three months from the registration of the return the company shall be deemed to be dissolved.

In the case of a dissolution by the court, when the affairs of a company have been completely wound up, the court, if the liquidator makes an application, shall make an order that the company be dissolved. A copy of the order is filed at the ROC which records the dissolution.

In the case of a reorganisation within the meaning of section 198 of the Companies Law an official copy of the order granted by the court must be delivered to the ROC otherwise it shall have no effect and a copy of every such order is annexed to every copy of the memorandum of the company issued after the order has been made. Furthermore, the provisions set out in the arrangement agreed between the companies in question must be performed.

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**International cases**
**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Cyprus has not enacted any separate law for the adoption of the UNCITRAL Model Law on Cross-Border Insolvency. However, since 1 May 2004 Cyprus is a full member of the European Union and therefore bound by the terms of Regulation 1346/2000.

Recognition of foreign insolvency proceedings in Cyprus can be effected through the following.

- Regulation 1346/2000, which is applicable to all member states except Denmark. The Regulation separates the possible insolvency proceedings that may be taken into two broad categories; the main insolvency proceedings and the secondary insolvency proceedings. The cornerstone for establishment of jurisdiction in the courts of one member state for the main proceedings is where the centre of a debtor's main interests are. Secondary proceedings may be opened subsequently to the main proceedings in another member state if the debtor has an establishment in the territory of this state. The Regulation provides that judgments handed down by a court whose judgment concerning the opening of proceedings is recognised in accordance with article 16 and that concern the course and closure of insolvency proceedings and compositions approved by that court shall also be recognised with no further formalities. Any member state may refuse to recognise insolvency proceedings



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opened in another member state or to enforce a judgment handed down in the context of such proceedings where the effects of such recognition or enforcement would be manifestly contrary to that state's public policy, in particular its fundamental principles or the constitutional rights and liberties of the individual.

- The Credit Institutions Reorganisation and Winding-Up Directive (2001/24/EC), which creates rules to ensure that reorganisation measures or winding-up proceedings adopted by the administrative or judicial authorities of the home state of an EU credit institution are recognised and implemented throughout the Community. The Directive provides that, with some exceptions, the national law of a credit institution's home state will apply in the event of a reorganisation or winding-up proceedings, including in respect of its branches in other member states.

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#### COMI

#### **48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

In accordance with Regulation EC 1346/2000 on Insolvency Proceedings, the 'centre of main interests' should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties. Article 3 of the Regulation provides that in the case of a company or legal person, the place of the registered office shall be presumed to be the centre of its main interests in the absence of proof to the contrary.

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#### Cross-border cooperation

#### **49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

EC Regulation 1346/2000 aims to create more efficient and effective cross-border insolvency proceedings in order to promote the proper functioning of the internal market.

The Regulation enables the main insolvency proceedings to be opened in the member state where the debtor has the centre of his main interests. These proceedings have universal scope and aim at encompassing all the debtor's assets. The Regulation permits secondary proceedings to be opened to run in parallel with the main proceedings.

The Regulation does not apply to insurance undertakings, credit institutions (including cooperative companies), certain investment undertakings and collective investment undertakings.

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#### Cross-border insolvency protocols and joint court hearings

#### **50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

Cyprus has not entered into any cross-border insolvency protocols or other arrangements that enable the court to coordinate proceedings with other countries or hold joint hearings. As a member of the EU, Cyprus applies Regulation 1346/2000 that aims to create a framework for the commencement of proceedings and for automatic recognition and cooperation between the different member states.

Provisions, however, do exist for cross-border mergers that require a certain level of communication/interaction between the relevant authorities of both member states in order for the procedure to be completed.

# Dominican Republic

Mary Fernández, Jaime Senior and Melba Alcántara

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

On 7 August 2015, a new law on Restructuring and Liquidation of Companies and Business Persons (Law No. 141-15) was signed into law in the Dominican Republic. Law No. 141-15 repeals and substitutes all laws and regulations on the matter prior to the same, and in particular, articles 437 to 614 of the Code of Commerce, as well as Law No. 4,582 on Declaration of Bankruptcy, which dates to 1956. Prior to the enactment of the new Law, it was not possible to request the reorganisation of the insolvent debtor in the Dominican Republic, given that all the laws applicable to insolvency proceedings solely referred to its liquidation. Note that as Law No. 141-15 will enter into effect as of 7 February 2017, the Code of Commerce and Law No. 4,582 on Declaration of Bankruptcy will remain in effect and apply to any insolvency proceedings prior to such time.

Under the terms of Law No. 141-15, a debtor could become subject to a restructuring proceeding – whether voluntary or involuntary – if one of the following conditions is met: failure to pay claims regarded as certain, due and payable under Dominican law for a period of more than 90 days, after formal notice to pay; when the debtor's current liabilities exceed the current assets for a period of more than six months; failure to pay withheld taxes to the tax authorities for a period of more than six fiscal quotas; failure to pay two consecutive salaries to employees on the corresponding payment date, with the exception of payments made in the hands of a third party when required by a court order, and of the 'economic assistance' set out by the Labour Code for businesses unable to produce funds; when the administration hides or remains vacant for a reasonable period of time and no officer is designated to comply with its obligations, suggesting the intention to deceive the creditors; when the closure of the business is ordered because of the absence of the administrators, as well as the transfer – partial or total – of its assets to a third party for distribution to all or some creditors; the use of deceitful or fraudulent practices, criminal association, breach of trust, falsehood, simulation or fraud to default creditors; the notification to creditors of the suspension of payments by the debtor, or of the intent to do so; the commencement of a foreign insolvency proceeding in the jurisdiction of the debtor's parent company or of its main place of business; the foreclosure of more than 50 per cent of the debtor's total assets; and the existence of decisions or sentence-enforcement procedures that may affect more than 50 per cent of the debtor's total assets.

Prior to the enactment of Law No. 141-15, the criterion to determine whether a debtor could become subject to bankruptcy proceedings revolved around the concept of 'cessation in payments' rather than considering a state of insolvency. Thus, a merchant or a commercial entity that discontinued payments might have very well been subject to a declaration of bankruptcy. The number and quantity of the debts owed were not the relevant factors established by law in considering whether a bankruptcy declaration may proceed.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Law No. 141-15 of 2015 creates a special jurisdiction for restructuring and judicial liquidation, comprising courts of first instance and courts of appeal, both of which will be specialised to hear restructuring and liquidation proceedings. However, until the new jurisdiction is created, the actions provided for in the law will fall within the jurisdiction of the ordinary civil and commercial courts.

The restructuring and liquidation courts will be competent to hear all actions related to the restructuring plan, as well as any other judicial or extrajudicial action linked to the debtor and its equity. The restructuring and liquidation courts will also be competent to hear all possible measures to preserve the debtor's assets, including petitions for precautionary measures and protective actions. Civil or criminal actions for non-compliance with the law shall be heard by the ordinary courts.

Under the previous legislation, bankruptcy proceedings were brought before the Civil and Commercial Chamber of the Court of First Instance. However, prior to bringing the claim to court, a mandatory conciliation proceeding governed by Law No. 4,582 had to take place before the Chamber of Commerce. Most attempted bankruptcy proceedings were settled at this stage and rarely continued to the litigation stage.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Law No. 141-15 applies to national or foreign companies and business persons with domicile or continuous presence in the country, and excludes commercial entities controlled by the state; financial intermediation entities regulated by the Monetary and Financial Law No. 183-02, dated November 2002, and its modifications; securities intermediaries, investment fund management companies, centralised security deposits, stock exchanges, securitisation companies and any other entity considered to be a stock market participant, with the exception of publicly traded companies and companies governed by Law No. 19-00 on Securities Market dated May 2000. Special rules apply to companies participating in the electric sector are also excluded.

Law No. 141-15 excludes the following assets from the bankruptcy proceedings: those which might be claimed by third parties in accordance with law; unregistered purchases of real property that remain unpaid; amounts related to tax withholdings; assets and rights owned by third parties in possession of the debtor; as well as personal belongings that are essential for the debtor's subsistence, and assets employed in the ordinary course of business. Additionally, Law No. 1,024 of 1928 provides that 'family property', once declared or converted as such, is not subject to attachment or foreclosure, even in cases of bankruptcy or liquidation.

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**Public enterprises**


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**4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?**

Law No. 141-15 excludes entities that are government owned or controlled. According to the Public Administration Organic Law No. 247-12, dated 14 August 2012, the suppression of government entities may only be decided by instruments with the same regulatory status as the one that created them. Government entities that are functionally decentralised may only be suppressed by law, which will provide the basic rules that will govern its dissolution as well as the necessary powers to the entity responsible for the liquidation.

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**Protection for large financial institutions**


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**5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?**

Dominican law does not specifically address the concept of 'too big to fail', but the Monetary and Financial Law, Law No. 183-02 of 2002, does have specific procedures related to the insolvency of financial institutions. The Superintendency of Banks, along with the Monetary Board of the Dominican Republic, is charged with the primary supervision and actions related to such procedures. Financial institutions facing economic difficulties must present a regularisation plan upon the occurrence of one of the following situations: a decrease of 10 per cent to 50 per cent of the value of their net equity within a period of 12 months; if the institution's solvency ratio falls below the coefficient required by law; deficiencies in the legal reserve during a number of periods established by law; repeated recourse to the Central Bank as a lender of last resort; the submission of false financial information or fraudulent documentation to the Superintendency of Banks or the Central Bank; the performance of transactions that seriously endanger public deposits or the institution's liquidity or solvency; among others. The Superintendency of Banks is required to render a decision with respect to the proposed regularisation plan within the five days following its presentation. The regularisation period may not exceed six months.

Failure to present the regularisation plan will lead to the dissolution of the financial institution, as well as any of the following causes: the rejection of the regularisation plan; a cessation of payments; a decrease of the solvency ratio 50 per cent below the coefficient required by law; carrying out operations during the execution of the regularisation plan that make the same unfeasible; failure to remedy of the causes that gave rise to the regularisation plan before the expiry of the term; and the revocation of the institution's authorisation (licence) to operate. The Central Bank also operates a contingency fund, funded from mandatory contributions of all financial institutions of the country, which guarantees deposits up to a certain amount and which may also be used to assist troubled institutions in limited circumstances.

In the case of failed banks, the Superintendency of Banks may resort to the securitisation regime foreseen in said Securities Market Law to implement the dissolution procedure. Securitisation of assets will require structures similar to investment funds, which will issue shares of several categories, granting various rights to its holders. Article 63, letters d and e, of Financial Law No. 183-02, was amended by Law No. 189-11 for the Development of the Mortgage Market and Trust in the Dominican Republic (Law No. 189-11), to include debt securities for construction and house financing as privileged obligations in light of a dissolution procedure of a banking entity.

The Dominican Social Security Law No. 87-01 provides that insurers and reinsurers operating in the local market may be subject to both voluntary and involuntary liquidation procedures. The involuntary liquidation shall occur when authorisation granted to the insurer or reinsurer is revoked because of failure to maintain the funds of the 'guarantee of profitability' account above 1 per cent of the total value of the pension funds, or when the minimum profitability of the fund is below the real profitability of the past 12 months and the pension fund manager is unable to cover the difference. In these cases, the Superintendency shall dissolve the entity without judicial intervention. Should dissolution or liquidation occur under other circumstances, the procedure established by Law No. 141-15 for companies and business persons will apply.

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**Secured lending and credit (immoveables)**


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**6 What principal types of security are taken on immoveable (real) property?**

The principal type of security on real property is the mortgage. Mortgages are governed by the general provisions set forth in articles 2114 et al of the Dominican Civil Code and by the Real Property Registration Law, Law No. 108-05 of 2005. The Dominican Civil Code defines a mortgage as a guaranty right over real property that guarantees the fulfillment of an obligation.

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**Secured lending and credit (moveables)**


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**7 What principal types of security are taken on moveable (personal) property?**

The principal type of security taken on moveable property under Dominican law is the non-possessory pledge. Similar to the chattel mortgage and originally intended for crops and agricultural equipment but later expanded to cover virtually all sorts of moveable assets, including industrial machinery and motor vehicles, this type of security is governed by the Agricultural Incentive Law No. 6,186 of 1963.

In addition to the above, pledges – generally governed by the provisions set forth in the Civil Code, and for transactions involving merchants, governed by the provisions of the Code of Commerce – may be granted over virtually any type of personal property, including intangible goods such as stock, securities, account receivables and industrial property rights. When a pledge over tangible assets is granted under the provisions set forth in either of the aforementioned codes, the pledgor is not allowed to retain possession of the asset.

A proposed bill that would modernise and introduce new credit possibilities for moveable property is soon to be presented before Congress.

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**Unsecured credit**


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**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

Before commencing any other action, an unsecured creditor can seek from the judge, in an *ex parte* proceeding, an order attaching personal property owned by his or her debtor. This right is granted to the creditor by article 48 of the Code of Civil Procedure, as amended by Law No. 845 of 1978. Most judges are lenient in granting this authorisation and base their decision primarily on the plaintiff's allegations, without demanding proof of the urgency or danger or questioning the *prima facie* validity of the claim, although the Supreme Court has repeatedly insisted that judges should do so. The claimant then asks a bailiff to serve a copy of that order on the debtor, in person or at his domicile. The bailiff seizes and removes assets of the debtor or obtains a commitment from the debtor or a third person that he or she will act as custodian of the assets that are listed on the bailiff's return. These assets are the security for the payment of the final ruling on the merits of the case. After the assets have been attached, the claimant has 30 days in which to file his or her action on the merits.

Prior to any insolvency proceedings, the claimant can also attach real property owned by the debtor in an *ex parte* pre-judgment proceeding pursuant to article 54 of the Code of Civil Procedure, except that if the property is the debtor's homestead, in accordance with Law No. 1,024 of 1928, it may not be attached. To attach real property, the creditor applies to the court for a provisional judicial lien, which when granted is filed at the Land Registrar's Office and is then notified to the debtor within the following 15 days. After the case on the merits is heard, if the plaintiff is successful, the provisional judicial lien is converted into a definitive judicial lien, which the plaintiff can then foreclose on the property in a separate proceeding.

Another possibility that the claimant may use (prior to the commencement of any insolvency proceedings) is that of garnishing a debt owed to his debtor by a third party. This possibility is known as an *embargo retentivo*. For a garnishment, the creditor needs a judicial authorisation only if his or her claim is for an indeterminate amount, for example, as damages for a personal injury or a breach of contract. If he or she holds an instrument giving a right against the debtor for the payment of a liquid sum, such as a promissory note, a dishonoured cheque, or an acknowledgment of the debt, then he or she need only join a copy

of that instrument to the notice of garnishment that the bailiff serves on the third party. Typically, the third party is a bank in which the debtor has funds on deposit.

After the enactment of Law No. 141-15, upon approval by court of the restructuring request, all judicial, administrative or arbitral decisions that affect the assets of the Debtor, any enforcement or eviction procedures regarding the Debtor's moveable and immoveable property, calculation of interest under loans and other credit documents, among others, are suspended.

According to Law No. 141-15, following the judgment ordering the liquidation of the debtor, the verification of unsecured claims will not occur in those cases where the judicial costs and secured claims completely absorb the product of the realization of the assets, except for businesses, in the cases where the administrators (remunerated or not) may be required to take charge over part or all the liabilities.

Foreign creditors have the same rights and can rely on the same remedies available to local creditors.

## Voluntary liquidations

### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Under Law No. 141-15, the debtor may request its judicial liquidation before the court at any moment. However, the person verifying the financial situation of the debtor, and the conciliator of the reorganisation, may recommend the immediate liquidation under specific circumstances (such as the refusal of the debtor to recognise the reorganisation requested by the creditors, the recommendation made by the creditor's representative, the non-approval of the reorganisation plan or failure to comply with the restructuring plan).

The notice of the judgment that orders a judicial liquidation entails that the debtor immediately loses all right to manage and dispose of all properties until the judicial liquidation process has concluded. The court must then designate a person who will act as the administrator of the liquidation process (the liquidator). The liquidator assumes the authority of the governing bodies. During the judicial liquidation process, the rights and actions of the debtor are exercised by the liquidator. Upon his appointment, the liquidator assumes all management functions and powers of the debtor. Likewise, for three consecutive days, the liquidator must publish in a newspaper of national circulation and on the webpage of the court an excerpt of the judgment that orders the liquidation, and must notify the judgment to the debtor and the creditors.

Prior to the enactment of Law No. 141-15, the debtor would pursue its liquidation amicably through the amicable settlement process governed by Law No. 4,582 of 1956. If such attempt was unsuccessful, the liquidation was brought to a judicial court.

## Involuntary liquidations

### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Law No. 141-15 establishes the obligation to attempt the reorganisation of the debtor prior to initiating involuntary liquidation proceedings. However, the person verifying the financial situation of the debtor and the conciliator of the reorganisation may recommend the immediate liquidation under specific circumstances.

The judicial liquidation of the debtor may be initiated by the verifier, if there is a lack of information or efforts to thwart the duties of the verifier by the debtor, or when the verifier determines that the debtor is not in a position that makes possible a restructuring process; by the conciliator during the phase of conciliation and negotiation, whether it is a result of the impossibility of assuming his or her functions because of the lack of cooperation by the debtor or a determination that the debtor will be unable to restructure; or by any of the debtor, the conciliator, any recognised creditor or by decision of the majority of creditor in the event of non-compliance with the terms of the restructuring plan. See question 9 for further information regarding the effects of the judgment that orders a judicial liquidation under Law 141-15.

Prior to the enactment of Law No. 141-15, only unsecured creditors could bring the liquidation action through judicial proceedings after attempting the amicable settlement process governed by Law No. 4,582 of 1956. Basically, a creditor with such interest was required to provide proof of the insolvency of the debtor or its general cessation of payment

of debts. The effects of the involuntary liquidation proceedings were the same as the ones for a voluntary liquidation process.

## Voluntary reorganisations

### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Law No. 141-15 contemplates the commencement of the insolvency proceedings by the Debtor at any moment (see question 1 for further information regarding the criteria to determine if a debtor is insolvent). Prior to the enactment of Law No. 141-15, the applicable laws dealt mainly with liquidation and did not contemplate reorganisation.

The restructuring of the debtor may be requested before the court through a petition. According to article 29 of Law No. 141-15, the restructuring request presented by the debtor voluntarily must be accompanied with the financial statements issued for the last three fiscal years; a report explaining the debtor's economic condition and justifying the need for restructuring; a list of all its creditors and the status of all its claims and liabilities (including date of approval and of expiration and a description of the collateral - if any); in the case of businesses, the authorisation of the management expressly approving the restructuring request; a detailed report of all judicial, administrative, labour, arbitral or any other action or procedure to which the debtor is a party; a certification issued by the tax authorities confirming that the debtor is up to date with its fiscal obligations; copies of bank account statements; among other documents.

Following the restructuring request, the court has the obligation to appoint a verifier within a period of three days, who will have the duty to verify the debtor's financial situation and inform the court thereof. The verifier may be assisted by experts on the matter and has ample powers to obtain information about the debtor's business, assets and liabilities and financial situation (in particular, about the assets of the debtor's business that are subject to the restructuring process, or the estate). The verifier is required to present his report to the court within 15 business days following his appointment. Within five business days following the presentation of the verifier's report, the court must decide whether to accept the restructuring request or deny the same.

In the event that the restructuring request is accepted by the court, then such decision must be duly notified to the debtor and the creditors. The court will then appoint a conciliator, whose principal role is to mediate between the debtor and its creditors in order to reach a restructuring plan. Furthermore, the court will order the publication of an excerpt of the restructuring request in a newspaper of national reach in the country as well as on the court's website.

Upon appointment of the conciliator, the conciliation and negotiation process is initiated. The law calls for the ordinary functioning of the debtor and his business during the conciliation process. During this process, the management of the debtor's assets continues to be handled by the debtor, but remains subject to the supervision of the conciliator. Likewise, during the conciliation, all judicial, administrative or arbitral decisions that affect the assets of the debtor, any enforcement or eviction procedures regarding the debtor's moveable and immoveable property, calculation of interest under loans and other credit documents, among others, are suspended.

The restructuring plan proposal must be presented for review and subsequent approval, or rejection, of the creditors. In the event that the creditors reject the proposal, the restructuring of the debtor may follow. However, if the restructuring plan proposal is approved by the creditors, it must be presented to the court for verification and subsequent approval. Once approved by the court, the conciliator is charged with overseeing compliance with the restructuring plan.

In addition, the law provides for 'pre-pack agreements', which may be presented if the debtor and the majority of his creditors reach a restructuring agreement prior to the commencement of the restructuring process. If this is the case, the debtor and the creditors must present said 'pre-pack agreement' to the court, which will reject any restructuring petition file with respect to the debtor for a period of 30 days following the request of the agreement. The 'pre-pack agreement' proposal must be accompanied by a proposal for appointment of a conciliator, which shall be designated by the court if the plan is accepted to oversee the execution of said plan. The approval of the 'pre-pack agreement' shall be notified to the debtor and the creditors, and will produce the same legal effects as a restructuring plan.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Pursuant to Law No. 141-15, the restructuring of the debtor may be requested before the court, through a petition, by any creditor who has an asset (liability in relation to the debtor) in an amount that exceeds 50 monthly minimum wages and if the debtor is facing any of the situations that can give rise to the right to petition under the Law (in particular, cessation of payments or any other event that leads a creditor to believe that the debtor is in a precarious financial situation). See question 1 for further information regarding the criteria to determine whether the debtor may be subjected to a restructuring request.

Creditors are required to present the before the court following documentation with their restructuring petition: a list of the creditors filing the request; identification of the debtor and a list of its offices or installations; a precise indication of the facts giving rise to the request; copy of the documents that verify the creditor's rights or assets; copy of the last financial statements (in the case of legal entities); a certification issued by the tax authorities confirming that the claimants are up to date with their fiscal obligations; and copy of the power granted on behalf of the creditor's representatives. In the case of foreign creditors, a local representative shall be designated.

Following the request, the court has the obligation to appoint a verifier within a period of three days, who will have the duty to verify the debtor's financial situation and inform the court thereof. Restructuring requests filed by the creditors must be notified to the debtor within a period of three business days following the filing date, and shall include all the documents presented to the court by the creditors. The creditors have the obligation to present proof of the notification before the court within a period of two business days; failure to do so entails the dismissal of the request.

In the event that the restructuring request is accepted by the court, a conciliator shall be appointed in order to reach a restructuring plan. During the conciliation process, the creditors must declare and supply to the conciliator the documents evidencing their assets (liabilities in relation to the debtor). After the conciliator verifies and confirms such liabilities, this portion of the conciliation process concludes with the publication of a final list of liabilities (subject to any annulment action that remains in course).

The restructuring plan proposal must be presented for review and subsequent approval, or rejection, of the creditors. In the event that the creditors reject the proposal, judicial liquidation of the debtor may follow. However, if the restructuring plan proposal is approved by the creditors, it must be presented to the court for verification and subsequent approval. Once approved by the court, the conciliator is charged with overseeing compliance with the restructuring plan.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

According to article 227 of Law No. 141-15, all persons who directly or indirectly administer, direct or liquidate, in fact or in law, a business subject to the Law, may face criminal prosecution and be subject to imprisonment of up to five years and penalties of up to 3,500 minimum wages. People responsible for the intentional delay of the procedure; the completion of fraudulent transactions for personal gains; the fraudulent reduction or increase of the debtor's assets; as well as the use of false accounting or separate bookkeeping, will be held criminally liable under the terms of the Law.

All transactions made while the debtor is insolvent will be declared null and void if the other party is aware of the general cessation of payment of the company. See question 39, below, for further information regarding transactions that may be annulled.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

Law No. 141-15 contemplates the possibility of carrying on business during reorganisation subject to the approval of the conciliator, who has the obligation to inform the court and the creditors of all issues regarding the administration of the debtor. During the negotiation phase of the proceedings, the debtor remains in possession of the business under the supervision of the conciliator, and may only dispose of the necessary assets for the ordinary course of business. However, the conciliator may remove the debtor from the administration of the business to protect the estate. In that same vein, the conciliator may initiate an annulment action against acts executed by the debtor undertaken within the two years prior to the restructuring request, when these have constituted an unjustified dissipation of the debtor's assets and have caused damage to the creditors. See question 39 for further information regarding transactions that may be annulled.

Under the terms of Law No. 141-15, new debts have a higher priority in relation to all other secured and unsecured claims of the debtor, with the exception of tax claims, employee claims, and claims resulting from the payment of the restructuring process, which are entitled to a higher priority status. See question 33 for further information regarding the higher priority of new debt under the terms of No. 141-15.

Upon approval of the restructuring request, the court will order the publication of an excerpt of the restructuring request in a newspaper of national reach in the country as well as on the court's website. Following the publication, the debtor has the obligation to file before the court a list of the providers or suppliers that are essential for the ordinary course of business. Such providers or suppliers are required to maintain the provision facilities during the restructuring of the debtor. Should the essential providers or suppliers refuse to continue supplying goods and services without adequate justification, the court may order the continuation of the supply for a reasonable period of time upon request of the conciliator. The definitive refusal to continue supplying goods and services after the commencement of the process may result in the declaration of such debt as unsecured credit.

Law No. 141-15 also includes the concept of post-filing debtor in possession (DIP) financing and establishes a priority for its payment. New financing must have the approval of the court and the petition presented by the conciliator may be objected by the creditors. The constitution of new financial collateral may also be authorised by the court, after hearing the creditors' adviser. New obligations will be ranked after existing privileges.

During the review of the restructuring request and for as long as the restructuring process is in course, the creditors have the right to appoint a physical or legal person to assume their collective representation during the procedures and actions provided for in the law (the creditors' adviser). Upon proposal of the conciliator and considering the position of the majority of creditors, the court must decide on the termination of existing contracts and the approval of new debt, the constitution of new collateral, the sale of assets and the disposal of assets that are not required for the ordinary course of business. Notices have to be given to creditors prior to the sale or disposition of assets, who may file their opinion through a written report within a period of 10 days. If an encumbered asset is sold, the secured creditors shall receive a proportion of the selling price. The court may authorise the immediate sale by the conciliator of perishable or depreciable assets. Creditors who represent at least 30 per cent of the claims may appeal the court's approval.

The conciliator has the faculty of convening meetings with the debtor's governing bodies when deemed necessary. If a meeting does not occur after two notices given to the corresponding body, the conciliator may take the judicial and extrajudicial actions necessary to request the replacement of the governing bodies of the debtor.

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**Stays of proceedings and moratoria**


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**15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

According to Law No. 141-15, upon initiation of the conciliation and negotiation process, all judicial, administrative or arbitral decisions that affect the assets of the debtor and any enforcement or eviction procedures regarding the debtor's property (moveable and immovable) are suspended until the reorganisation plan is approved. However, the debtor's obligations to support their families and children (in the case of natural persons); labour and social security obligations; and payments made as a result of the ordinary course of business, will not be suspended. Definitive judgments awarding money damages are also excluded from the stay, provided that they are not susceptible of being annulled, as well as legal actions concerning securities of public offering originated prior to the restructuring request with subsequent settlement date.

Unless the judge opposes to a claim, it will remain enforceable after the commencement of the reorganisation proceedings; if contract is extended, such claims are treated as new debts and therefore acquire a higher priority in relation to other claims. See question 33, below, for further information regarding the higher priority of new debt under the terms of Law No. 141-15.

Secured claims that benefited from collateral during the 'suspect period' may be subject to the invalidation of such collateral. However, bona fide pledgees may oppose the return of the asset until the secured obligation and any accessory rights are repaid or exchanged for equivalent collateral. See question 39, below, for further information regarding transactions that may be annulled.

Pursuant to article 149 of the law, the judgment that orders a judicial liquidation overturns the stay of all legal proceedings and resumes all actions against the debtor.

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**Post-filing credit**


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**16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

Upon the request of the conciliator, and provided there is no objection from the majority of creditors, the court may authorise new super-senior financing on account of the debtor, in order to assure the continuity of the ordinary operations of the debtor. The law establishes a priority for the payment of post-filing credit, which must be requested by the conciliator with the approval of the court; the petition may be objected to by the creditors. See question 33, for further information regarding the higher priority of new debt under the terms of Law No. 141-15.

Prior to the enactment of Law No. 141-15, the debtor could not contract any further obligations. However, the liquidation administrator could incur further debt towards the continuation of a bankrupt business in the interest of unsecured creditors.

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**Set-off and netting**


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**17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

Law No. 141-15 contemplates the right of set-off and establishes the inclusion of alternative payment proposals in the restructuring plan, such as the conversion of debt into shares, participation loans and netting of claims, provided that the terms of the latter are agreed prior to the initiation of the conciliation and negotiation process. In addition, the stay of all proceedings caused by the declaration of liquidation by a judge does not affect the offsetting of credits.

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**Sale of assets**


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**18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

Law No. 141-15 contemplates the possibility of selling assets during the execution of the reorganisation plan for the purpose of allowing the debtor to satisfy its financial obligations as well as the continuation of its business. The court can approve the sale of assets that are perishable when abstaining from their sale would be harmful to the creditors of the bankrupt debtor. However, the conciliator may initiate an annulment action against acts that have constituted an unjustified dissipation of the debtor's assets and have caused damage to the creditors. See question 14 for further information regarding the conditions that apply to the use or sale of the assets of the business and question 39 for further information regarding transactions that may be annulled.

The awarding of assets approved by court is admitted during the conciliation and negotiation process, which entails the cancellation of any existing mortgages and the passing of assets 'free and clear'. According to article 177 of Law No. 141-15, the court can approve the amicable awarding of assets during the liquidation procedure, subject to further bids are contemplated in the liquidation plan. Any assets acquired would be passed 'free and clear' to the purchaser, except in connection with property that is subject to a lease. The initiation of the restructuring or liquidation of the debtor does not imply the termination of the lease agreements, which must be requested before the court through a petition. Penalties for anticipated termination of the lease and overdue rents corresponding to the last 12 months have higher priority in relation to other claims of the debtor.

Stalking horse bids in sale procedures and credit bidding in sales are not expressly contemplated by the law. However, the inclusion of alternative payment proposals in the restructuring plan is allowed. Provided that the creditor has been recognised (that is, that the credit has been duly verified and confirmed by the conciliator) and the claim has not been classified as subordinate because of the assignee's relation to the debtor, the credit bidder shall be permitted to bid in sales.

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**Intellectual property assets in insolvencies**


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**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

There are no provisions regulating this particular matter in the relevant legislation. The agreement that grants the rights over IP will usually prevail and parties will be bound by the terms of the agreement in question. However, upon proposal of the conciliator and considering the position of the majority of creditors, the court may decide to terminate any existing contract.

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**Personal data in insolvencies**


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**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Pursuant to article 61 of Law No. 141-15, during the phase of conciliation and negotiation, the conciliator has the right to obtain from public organisms all necessary information to achieve its objectives. In cases where the lifting of the bank secrecy is required, the conciliator may request that the court request the protected information through the mechanisms established by law. Additionally, the conciliator may file a written petition through the court requesting access to all information about the debtor that may be in possession of third parties, such as clients, suppliers, providers and credit information societies, provided that the information is necessary for the exercise of its duties

and achievement of its objectives. Pursuant to the terms of the Law, access may only be granted with respect to information necessary for the insolvency process.

### Rejection and disclaimer of contracts in reorganisations

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

Law No. 141-15, establishes the invalidity of contracts, which within 60 days prior to the commencement of the negotiation phase, or after the initiation of the proceedings, aggravate the situation of the debtor or accelerate the enforceability of claims not due. Additionally, pursuant to the terms of the said Law, no legal provision or contractual clause could give rise to the division, termination, resolution or annulment of the contract solely because of the acceptance of a reorganisation request or designation of the conciliator.

### Arbitration processes in insolvency cases

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Under Law No. 141-15, any controversy arising in the course of a restructuring procedure, or derived from the execution of the restructuring plan, may be subject to resolution before institutional or ad hoc arbitration. The request for arbitration will not be a cause per se for the suspension of the restructuring process. Administrative actions related to the restructuring, as well as all actions related to the liquidation, shall remain within the exclusive jurisdiction of a special court.

Prior to the enactment of Law No. 141-15, arbitration was not available for insolvency proceedings under Dominican law.

### Successful reorganisations

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

During the conciliation process, the creditors must declare and supply to the conciliator the documents evidencing their assets (liabilities in relation to the debtor). After the conciliator verifies and confirms such liabilities, this portion of the conciliation process concludes with the publication of a final list of liabilities (subject to any annulment action that remains in course). Once the liabilities have been verified, the restructuring plan must be presented.

The restructuring plan proposal must be presented for review and subsequent approval, or rejection, of the creditors. In the event that the creditors reject the proposal, judicial liquidation of the debtor may follow. However, if the restructuring plan proposal is approved by the creditors, it must be presented to the court for verification and subsequent approval. Once approved by the court, the conciliator is charged with overseeing compliance with the restructuring plan.

For purposes of a plan, creditors are classified as secured, unsecured and subordinated. Subordinated creditors are defined as those holding claims contractually defined as such; interest claims, excepting those payable under secured credit; claims for fines and penalties; claims owed by a related entity; and claims resulting from the cancellation of a transaction. The restructuring plan will contain, at least, the debtor's background; a summary of the restructuring plan, with a clear description of its main characteristics; information concerning the financial situation of the debtor; non-financial information of the debtor that may impact its future activity; a description of the future operations of the debtor and the effects of the restructuring; potential financial needs and the costs related to the proceedings; and a payment plan for the company's liabilities and the company's business plan for at least the following five years.

The restructuring plan can be organised through the constitution of a trust formed in accordance to the provisions of Law No. 189 on the Development of the Mortgage Market and Trusts in the Dominican Republic.

### Expedited reorganisations

- 24 Do procedures exist for expedited reorganisations?**

Law No. 141-15 establishes a special expedited procedure for restructuring where the total liabilities of the debtor do not exceed 10 million pesos, and where the time frames in court are reduced by half. In these cases, the minimum total liabilities to give rise to the right to file a request for restructuring is in an amount of at least 15 times the minimum monthly wage. The appointment of advisers for the creditors or expert and auxiliaries for the conciliator will not be applicable.

Prior to the enactment of Law No. 141-15, Dominican legislation did not contemplate the possibility of expedited reorganisations.

### Unsuccessful reorganisations

- 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

The restructuring plan proposal must be presented for review and subsequent approval, or rejection, of the creditors. In the event that the creditors reject the proposal, judicial liquidation of the debtor may follow. According to Law No. 141-15, the debtor may request its judicial liquidation before the court at any moment. In addition, the person verifying the financial situation of the debtor, and the conciliator, may recommend the immediate liquidation under specific circumstances, such as the refusal of the debtor to recognise the restructuring requested by the creditors, the recommendation made by the creditor's representative, the non-approval of the restructuring plan or failure to comply with the restructuring plan.

See question 10 for further information regarding the involuntary liquidation of the debtor.

### Insolvency processes

- 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

The law provides mechanisms for the participation by interested parties in the restructuring process. In that sense, during the review of the restructuring request and for as long as the restructuring process is in course, the creditors have the right to appoint the creditors' adviser, a physical or legal person to assume their collective representation during the procedures and actions provided for in the law. The creditors of securities of the debtor issued in a public offering can also appoint a representative known as the 'representative of publicly issued securities'. Likewise, the employees of the debtor may also appoint a person who will act in the capacity of adviser for the employees (the employees' adviser). Advisers represent the collective interests of the respective interested groups with priority over other interested parties during the restructuring process. However, in cases where advisers are not appointed, or are appointed and then removed, their duties and obligations will correspond to the creditors or employees.

The creditors' adviser has the obligation to inform creditors of all actions concerning the restructuring process; to assess the creditors on the approval of the restructuring plan proposals, the reports for the constitution of new credit, off-setting of credits and the constitution of collateral; request any information that may affect the creditor's rights through a written petition, among others.

Notices shall be given to creditors prior to the sale or disposition of assets, who may file their opinion through a written report within a period of 10 days. Creditors have the right to request all the information they deem necessary to evaluate the proposed restructuring plan. After the liquidation plan is decided, the liquidator has the obligation to inform the court and the creditors, via the creditors' adviser, of its compliance.

Upon petition of any creditor, the creditor may request the annulment of transactions made within a period of two years prior to the filing date of the reorganisation request, provided that the court deems they constitute an unjustified diversion of assets or are detrimental to creditors. See question 39 for further information regarding transactions that may be annulled. The plan may provide for the cancellation of fiscal debt by the tax authorities.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Law No. 141-15 contemplates the possibility of recovering moveable assets in favor of the estate, provided that their sale was resolved prior to the commencement of the reorganisation or a by a judicial decision rendered afterwards. In the case of assets sold by the debtor that remain unpaid, the creditors may subrogate in the rights of the debtor as the legitimate owners against the third-party purchaser.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The law provides mechanisms for the participation by interested parties in the restructuring process. Creditors and employees have the right to appoint advisers, who represent the collective interests of the respective interested groups with priority over other interested parties during the restructuring process. The advisers are appointed by majority voting. See question 26 for further information regarding the representatives appointed by the parties and their functions.

Decisions are made by the creditors with a minimum of 60 per cent of favourable votes. Each registered or recognised creditor has the right to one vote per every 1 per cent (or portion higher than 0.5 per cent) of the total registered debt to which he or she is entitled. Except when there is only one creditor, one registered or recognised creditor cannot hold more than 50 per cent of the votes, regardless of the sum of their claim.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

There are no special provisions regarding insolvency proceedings of a corporate group. In principle, separate proceedings will take place for each entity comprising the corporate group.

Law No. 141-15 sets forth a legal framework applicable to insolvency proceedings with international or cross-border effects, developed in accordance with the United Nations Commission on International Trade Law (UNCITRAL). Upon recognition of the foreign procedure, the foreign representative may request the court the appointment of an officer for the distribution of all or part of the estate located in Dominican territory, provided that the court assures the protection of the rights of Dominican creditors.

No provisions exist either in relation to the transfer of assets between administrations appointed in different jurisdictions. Given that insolvency in the Dominican Republic is ruled by the territoriality principle, the enforcement of a consolidation of proceedings in different countries is unlikely. Proceedings in the Dominican Republic will only affect assets located in the Dominican Republic as the territoriality principle will also bar a local administration from exercising jurisdiction abroad.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Pursuant to Law No. 141-15, the appellant has an automatic right to appeal those decisions whose review is permitted by the law. Decisions must be appealed within a period of 30 days following their notification, unless specifically stated otherwise by the Law. The placement of security is not required.

Decisions issued by the courts of first instance may be appealed to the restructuring and liquidation courts of appeal. These judgments may then be appealed to the Supreme Court of Justice. Decisions rendered by the Supreme Court only analyse the correct application of the law, and may confirm the appealed judgment or remand it for reconsideration by another court of equal hierarchy. Ultimately, should a party be unsatisfied with the said decision, it may be appealed to the Supreme Court of Justice for a second time. At this stage, the Supreme Court may confirm the decision or reach a new decision without need to remand to a different court.

In accordance with article 51 of Law No. 141-15, the decision of the court that accepts or denies the restructuring request may be appealed by any party within a period of 10 days following its notification. Considering that the appeal of the decision does not suspend the initiation of the phase of conciliation and negotiation, precautionary measures and protective actions may be taken by the court. In accordance with article 80 of the Law, creditors who represent at least 30 per cent of the claims may appeal the court's decision to authorise the immediate sale of depreciable assets by the conciliator.

Article 143 of the Law states that all decisions adopted by the court in connection with the execution or the amendment of the restructuring plan are subject to appeal. In addition, the decision of the court that accepts or denies the liquidation plan may be appealed within a period of five days following its notification. In accordance with article 193 of the Law, the following decisions are also subject to appeal: those that refer to the acceptance of the liquidation procedure may be appealed by the debtors; those that refer to the expiration of the recognition of claims may be appealed by the creditors; and those that refer to the restructuring plan and the liquidation procedure, may be appealed by the debtor, the creditors and the employees' adviser. Any other decision may be appealed by any party with legal capacity and legally protected interest.

Article 193 of the Law states that appeals do not suspend the ongoing procedure. However, the appellant may request the suspension of the matters decided by the appealed decision before the presidency of the Court of Appeals.

See question 2 for further information regarding the courts involved in the insolvency process. See question 31 for further information regarding the appeal of decisions related to a creditor's claims.

### Claims

#### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Upon approval of the restructuring request, the court will order the publication of an excerpt of the restructuring request in a newspaper of national reach in the country as well as on the court's website. Following the publication, the appointed conciliator must give notice to creditors within a period of one business day. The creditors may apply for a review of the approval within a period of 10 days following its notification. The recourse shall be notified to the other parties within a period of five business days from the filing date.

Law No. 141-15 establishes a period of 30 business days following the publication of an excerpt of the restructuring request for creditors to present their claims. Claims that are not presented within this deadline may present a tardy declaration at his cost, unless the creditor proves that his failure to notify was because of force majeure. The court must decide on the late declarations within a period of 20 business days.

The submission of claims can be made by the creditor or any representative, and must include general information of the debtor; the elected domicile for purposes of the receipt of notices given as a result of the restructuring procedure, or any alternative means of communication such as fax or an email; the amount of the claim with indication of the debt maturity date; the ranking of the claim; information on any other administrative, judicial or arbitral proceeding initiated with respect to the claim; and a declaration of the creditor on the existence of the claim, in the absence of an enforceable title. Claim submissions must be accompanied by copies of all the supporting documentation (whose originals may be requested by the conciliator). Claims in foreign currency shall be verified and paid in the currency agreed upon.

The conciliator must decide on the recognition of claims for contingent or unliquidated amounts. Pending obligations shall be met by the debtor unless the court decides otherwise. If contract is extended, such claims are treated as new debts and therefore acquire a higher priority in relation to other claims.

Questioned or disallowed claims are subject to judicial proceeding in which the interested parties may file evidence of their claims and legal arguments for their admittance within a period of 10 days after notices made via a national newspaper.

According to article 181 of Law No. 141-15, upon initiation of the liquidation procedure, and prior to admission of their claims, creditors with a special privilege of a lien or a mortgage, and the tax administration, may execute their individual rights if the liquidator has failed to initiate the liquidation procedure within a period of 45 business days following the date of the judgment that establishes the definitive list of credits.

#### Modifying creditors' rights

##### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

Under the terms of Law No. 141-15, new debts have a higher priority in relation to all other secured and unsecured claims of the debtor, with the exception of tax claims, employee claims, and claims resulting from the payment of the restructuring process, which are entitled to a higher priority status. See question 33 for further information regarding the higher priority of new debt under the terms of Law No. 141-15.

Secured claims that benefited from collateral during the 'suspect period' may be subject to the invalidation of such collateral. See question 39, below, for further information regarding transactions that may be annulled.

#### Priority claims

##### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Under the terms of Law No. 141-15, new debts have a higher priority in relation to all other secured and unsecured claims of the debtor, with the exception of tax claims, employee claims, and claims resulting from the payment of the restructuring process, which are entitled to a higher priority status.

According to article 86 of the law, the payment of debts must be carried out in the order described below:

- labour liabilities, if the same have not been advanced in application of the Labour Code or other laws related to social security or the employee's health;
- the costs of the restructuring process, including fees of officials and auxiliaries involved in the process;
- the loans agreed to by financial intermediation entities or third parties that will contribute to financing of the debtor, and which have been duly authorised by the court;
- the debts owed to essential and public service providers or suppliers, duly authorised by the court;
- the debts that result from the execution of agreements that remain in force after the beginning of the restructuring process, with respect to which the creditor in question agrees to receive deferred payment; and
- other liabilities, according to their rank under law.

Penalties for anticipated termination of lease agreements and overdue rents corresponding to the last 12 months also have higher priority in relation to other claims.

#### Employment-related liabilities in restructurings

##### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

According to Law No. 141-15, the termination of an employee during a restructuring or liquidation shall comply with the provisions of the applicable labour legislation. Upon termination, employees would be entitled to full payment of their severance unless, concomitantly with the insolvency proceedings, a separate process is conducted under article 82, section 5 of the Labour Code, which sets out the rules allowing a business to shut down and terminate its employees upon payment, as severance, of an 'economic assistance' amount, which is considerably lower than the termination payment that would otherwise be paid.

The conciliator must give notice to the employees' adviser of the verified labour credits within a period of 15 days following the publication of an excerpt of the restructuring request in a newspaper of national reach. Once the employees' adviser verifies the list, it must be notified to the Ministry of Labour and published on the website of the court. Employees whose claims are not included in the list presented by the conciliator may present their claims before the court within a period of 15 days following the notification made by the conciliator to the employees' representative.

#### Pension claims

##### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Pension-related claims arising from the restructuring or liquidation of the employer are not specifically regulated by Dominican insolvency legislation. In the case of failed pension funds, the Dominican Social Security Law No. 87-01 contemplates the intervention of the Superintendence of Pensions, which is required to proportionally allocate the employee's contributions to the rest of the pension fund managers.

See question 5 for further information regarding the insolvency of insurers and reinsurers operating in the local market. See question 34 for further information regarding employment-related liabilities.

#### Environmental problems and liabilities

##### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

There are no provisions regulating this particular matter in the relevant legislation.

#### Liabilities that survive insolvency proceedings

##### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

The debtor's liabilities may survive the restructuring of the debtor upon the final conclusion of the proceedings, as established in the restructuring plan. See question 23 for mandatory features of the restructuring plan. See question 33 for further information regarding the order for the payment of debts under Law No. 141-15.

#### Distributions

##### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Law No. 141-15 establishes that distributions will be made on a pro rata basis, after deducting from the realisation value of the assets the costs of the proceedings and the amounts paid to privileged creditors. See question 33 for further information regarding claims entitled to priority

### Update and trends

As discussed earlier, on 7 August 2015, a new Law on restructuring and insolvency (Law No. 141-15) was signed into law in the Dominican Republic. The Law is discussed in greater detail throughout this chapter. The Law will enter into effect on 7 February 2017.

status. If encumbered assets are sold, the secured creditors shall receive a proportion of the selling price.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

Law No. 141-15 contemplates the possibility of requesting annulment of transactions made within a period of two years prior to the filing date of the reorganisation request, provided that the court deems they constitute an unjustified diversion of assets or are detrimental to creditors. However, contracts on securities of public offering originated prior to the restructuring request and with subsequent settlement date are not subject to this annulment procedure.

The Law expressly declares several transactions as null and void, such as transfers of assets free of charge or at a price below market value; when the intended consideration is worth less than the obligation performed, or vice versa; the cancellation or partial or total relief of debt by the debtor; the grant of guarantees or the increase of the value of guarantees approved prior to the initiation of the proceeding without reasonable consideration; payments of obligations not yet due; transfers of property in favour of creditors which result in the payment of a higher amount to that received as a result of the liquidation; transactions with related entities or companies where the debtor or any of the creditors serve as an administrator or are part of the administering body, represent (jointly or separately) at least 51 per cent of the subscribed and paid-in capital, hold decisive power at the shareholder assemblies or are in the position to name the majority of the members of the governing body; transactions with related entities or companies where the debtor, its administrators, shareholders or directors represent, jointly or separately, at least 30 per cent of the subscribed and paid-in capital, hold decisive power at the shareholder assemblies or are in the position to name the majority of the members of the governing body among others.

Should the debtor be a natural person, the Law expressly declares several transactions as null and void, such as negotiations with the spouse or partner, people with whom the debtor coexists, or with whom the debtor has procreated, or their descendants, ascendants, or related collaterally or by affinity; and transactions with commercial entities where any of the previously cited people are administrators, serve as an administrator or as part of the administering body, or represent (jointly or separately) at least 51 per cent of the subscribed and paid-in capital, hold decisive power at the shareholder assemblies or are in the position to name the majority of the members of the governing body.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The law provides that transactions may be attacked before the court by the conciliator at the request of any creditor. Voidable transactions may be attacked upon initiation of the reorganisation proceedings. See question 39 for further information regarding transactions that may be annulled.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Law No. 141-15 also establishes the liability of officers for failure to meet the requirements established by law for the execution of their duties. According to article 223, the officers in charge of the restructuring or liquidation procedures who act in violation of the restraints, incapacities, constraints and disabilities established by the law, may face criminal prosecution and be subject to imprisonment of up to two years and penalties of up to 1,250 minimum wages. The officers found guilty of such acts shall be condemned to interdiction to exercise any function in any procedure established by the law for a period of five years from the definitive decision; and the interdiction to act as an administrator for a period of five years from the definitive decision.

Additionally, corporate officers and directors may be liable for labour claims and tax claims. Their liability may also be established upon their violation of criminal provisions relating to bankruptcies. If directors of a corporate bankrupt entity have been careless in the operation of the business and the keeping of its accounts or have concealed assets or engaged in other inappropriate conduct, they may become liable for criminal bankruptcy. Administrators of insolvent entities that act carelessly in the operation of the business may also be liable.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

There are no provisions under Dominican law regarding the effects of insolvency proceedings on subsidiaries or affiliates of the debtor under the current regime. Insolvency procedures of subsidiaries and affiliates would be treated as separate procedures, since there are no provisions regarding substantive consolidation or joint administration of related restructuring proceedings.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Law No. 141-15 expressly declares that transactions made with entities in which the debtor or its directors represent, jointly or separately, at least 30 per cent of the capital of the company or have decision-making authority are to be considered null and void. See question 39 for further information regarding transactions that may be annulled.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

There are no processes by which some or all of a business's assets may be seized outside of court proceedings, except for such pre-judgment liens explained above, as available remedies to all creditors.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Yes, there are extrajudicial proceedings for the liquidation of a corporation. This is done by the decision of the shareholders through fulfilment of formalities set forth in the by-laws of the corporate entity. If the by-laws are silent on this procedure, the shareholders designate the person in charge of the arrangements of said dissolution and liquidation. The dissolution is usually decided by a general extraordinary assembly in which the shareholders decide to put an end to the existence of the company and appoint a liquidator, who is in charge of managing the debts and assets of the company.

The main difference between the private liquidation of a corporation and liquidation under insolvency proceedings is that unpaid claims

may still survive a private liquidation; the dissolved company will be considered a de facto entity for such purposes.

#### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Reorganisation cases are formally concluded with the fulfilment of the reorganisation plan. Failure to comply with the terms of the reorganisation plan entails the initiation of the liquidation procedure.

#### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

Law No. 141-15 sets forth a legal framework applicable to insolvency proceedings with international or cross-border effects, developed in accordance with the United Nations Commission on International Trade Law (UNCITRAL). The law provides that foreign creditors have the same rights and can rely on the same remedies available to local creditors.

Upon filing of the application for recognition of the foreign proceeding, all judicial, administrative or arbitral decisions that affect the assets of the debtor and any enforcement or eviction procedures regarding the debtor's property (moveable and immoveable) are suspended until the court reaches a decision. The application for recognition of the foreign insolvency proceeding must be decided by the court within a period of 15 business days from the filing date. From the date in which the recognition of the foreign proceeding is requested, the foreign representative may request the appointment of an officer by the court for the distribution of all or part of the estate located in Dominican territory, provided that the court assures the protection of the rights of Dominican creditors. In addition, the foreign representative may request the verifier, conciliator or liquidator, the recovery of assets that belong to the estate, and the annulment of acts that have constituted an unjustified dissipation of the debtor's assets and have caused damage to the creditors.

As a result of the recognition of a foreign main proceeding, only one local restructuring procedure can be initiated. The effects of said procedure are limited to the assets located in the Dominican territory, and other assets that pursuant to Law No. 141-15 shall be administered in accordance with the law.

#### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

According to article 206 of Law No. 141-15, the debtor's COMI will be deemed its domicile for the purpose of the law, unless proven otherwise. The COMI is the centre of main interest of the debtor, or the place where the administration of its interests is conducted on regular basis and is accepted by third parties. In the case of natural persons, the debtor's domicile is the place of habitual residence.

The Dominican Tax Code provides that for tax purposes, business entities may be considered domiciled in Dominican territory when their COMI is located in the country, or its effective centre of management. COMIs are regarded as permanent establishments for income tax purposes.

#### Cross-border cooperation

#### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Law No. 141-15 contemplates the possibility of processing local and foreign insolvency proceedings simultaneously, in which case the local court shall collaborate and coordinate its actions with the foreign proceeding. See question 47 for further information regarding international insolvency proceedings.

There is no precedent that we are aware of concerning refusal to recognise foreign proceedings or awards. Nonetheless, in accordance to Dominican laws a judgment or award by a foreign court shall be enforceable in the Dominican Republic through an exequatur, authorising the validity of the foreign judgment. Dominican courts will ratify such judgment if it complies with all formalities required for the enforceability thereof under the laws of the foreign country; has been translated into Spanish, together with related documents and satisfies the authentication requirements of Dominican law; was issued by a competent court after valid service of process upon the parties to the action; was issued after an opportunity was given to the defendant to present its defence; is not subject to further appeal; and is not against Dominican public policy.



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**Cross-border insolvency protocols and joint court hearings**

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- 50** In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

Law No. 141-15 contemplates the possibility of processing local and foreign insolvency proceedings simultaneously. To the best of our knowledge, no joint hearings have been held by Dominican courts with courts in other countries. See questions 47 and 49 for further information regarding the recognition of insolvency proceedings in other countries.

# England & Wales

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

#### General insolvency legislation

The legislation principally applicable to the insolvency of companies incorporated in England and Wales is the Insolvency Act 1986 (the Insolvency Act) as amended from time to time. The Insolvency Act is supplemented by subordinate legislation, the most important of which are the Insolvency Rules 1986 (the Insolvency Rules). The Company Directors Disqualification Act 1986 (the CDDA 1986) deals with the position of directors of insolvent companies.

In relation to reorganisations, the Companies Act 2006 is also relevant as this sets out the provisions concerning schemes of arrangement (discussed further in question 11 below).

As at the time of writing, the UK remains part of the European Union, and, hence, the EC Regulation on Insolvency Proceedings 2000 applies (see also 'Update and trends'). This affects cross-border insolvencies and is discussed in more detail in questions 29 and 47 and the chapter on the European Union. The Cross-Border Insolvency Regulations 2006 (which incorporated into English law the UNCITRAL Model Law on Cross-Border Insolvency) are also relevant and are discussed in question 47.

On 25 May 2016, the UK government issued a consultation paper 'A review of the corporate insolvency framework – options for reform'. The consultation focuses on four areas:

- the creation of a new moratorium: This will provide companies with a moratorium on creditor action, initially of three months, subject to eligibility and qualifying conditions, with some supervision by an insolvency practitioner;
- helping businesses to continue to trade through a restructuring process: Providers of supplies essential to the particular business may be compelled to continue to supply, on the same terms as previously, and notwithstanding any contractual termination rights, through any moratorium and subsequent administration or company voluntary arrangement;
- developing a flexible restructuring plan: Proposals to allow stakeholders (including secured and unsecured creditors) to be crammed down across classes if they receive no less than in a liquidation; and
- exploring options for rescue financing: The consultation discusses whether to allow companies to grant security interests, during administration and other rescue processes, which could have priority (super-priority) over existing security (including prior fixed charges), subject to the creation of safeguards for existing secured creditors, and on allowing rescue financing to take priority over administration expenses.

The consultation closed on 6 July and the UK government intends to publish a response within three months thereof and, depending on the outcome, will bring forward final proposals for legislation as soon as parliamentary time allows. Should the government implement some of these reform suggestions, they will impact the insolvency landscape (and answers to some of the questions in this chapter) quite

dramatically. Where relevant, we have referenced the consultation in the questions where the topic may be impacted.

#### Determining whether a debtor is insolvent

'Insolvency' itself is not defined by the Insolvency Act. Instead the Act contains the concept of a company being 'unable to pay its debts'. A company is deemed to be unable to pay its debts if:

- it has not paid a claim for a sum due to a creditor exceeding £750 within three weeks of service of with a written demand in the prescribed form (known as a statutory demand);
- an execution or judgment against the company is unsatisfied;
- it is proved to the satisfaction of the court that it is unable to pay its debts as they fall due, also having regard to contingent and prospective liabilities, (generally known as 'cash flow insolvency'); or
- if it is proved to the satisfaction of the court that the value of the company's assets are less than the amount of its liabilities, taking into account contingent and prospective liabilities, (commonly known as the 'balance sheet test'). The highest court in England, the Supreme Court, held in *BNY Corporate Trustee Services Ltd v Eurosail UK 2007-3BL plc* [2013] UKSC 28 that the court is required to make an assessment of the company's assets and liabilities and to decide whether, on the balance of probabilities (making proper allowance for contingent and prospective liabilities), the company cannot reasonably be expected to meet those liabilities.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

There are no courts that deal solely with insolvency procedures. The High Court can wind up any company incorporated in England and Wales (and in some cases, foreign companies – see question 3). Any criminal matters must be dealt with by the relevant criminal court.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Generally, registered companies incorporated in England and Wales and companies formed outside England and Wales with their centre of main interests (COMI) in England and Wales can be subject to all forms of insolvency proceedings. Within the Insolvency Act there are separate provisions regarding the winding up of unregistered companies, which also apply to unregistered associations, friendly societies and foreign companies (provided they have sufficient connection with the jurisdiction).

The insolvency of partnerships (other than limited liability partnerships) is dealt with by the Insolvent Partnerships Order 1994 (as subsequently amended). Limited liability partnerships are subject to the Insolvency Act and related subordinate legislation subject to exceptions.

### Special regimes

In addition, there are special insolvency proceedings in respect of companies belonging to certain key industries. There are no fewer than 17 tailor-made insolvency regimes. The aim of the special regimes is to ensure the continuity of service and the orderly wind down and hand over of service provision where the services form an essential part of the country's infrastructure or are systemically important.

Legislation also exists that is designed to protect the financial markets from the insolvency of a market participant. This disapplies to a certain extent the general insolvency law and introduces specific provisions. This area is a highly complex and deeply regulated area. Key legislation governing the issue is Part VII of the Companies Act 1989 and Part XXIV of the Financial Services and Markets Act 2000 (as amended) as well as subordinate legislation.

Regulated entities, such as financial institutions, are supervised and regulated by two regulatory bodies, the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA), which are each given specific powers to apply for and participate in the application for the insolvency of a regulated entity.

Further, there are certain legislative measures taken at the European Union level (which are transposed into English law) regulating in which country within the European Union an insurance company or credit institution ought to be wound up. These are the Insurers (Reorganisation and Winding up) Regulations 2004 (implementing Council Directive 2001/17 EC on the reorganisation and winding up of insurance undertakings) and the Credit Institutions (Reorganisation and Winding Up) Regulations 2004 (implementing Council Directive 2001/24 EC on the reorganisation and winding up of credit institutions). The aim of these two regulations is to provide greater consumer protection and to achieve a consistent approach to insolvency proceedings across the European Union.

### Excluded assets

All property in which the company has a beneficial interest will fall within the insolvent estate and be available for the benefit of creditors. Assets subject to a fixed charge, supplied under hire purchase agreements, subject to retention of title claims (see question 8) or which the company holds on trust for a third party are not beneficially owned by the company and therefore do not fall within the insolvent estate, subject to such claims being valid, and in the case of a trust, the trust being properly constituted.

### Public enterprises

#### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There are no specific rules for government-owned enterprises and the normal rules on insolvency applicable to the type of company involved apply. As noted in question 3, there are special insolvency proceedings regarding of companies belonging to key industries and these special insolvency proceedings will often provide for the government or a particular department or agency to be involved in the process. Creditor remedies are therefore also as provided in the respective insolvency proceeding.

### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Yes. The Banking Act 2009 (the Banking Act), which came into force on 21 February 2009 (as amended), governs the rescue or wind down of banks and other financial institutions. The Banking Act establishes a permanent special resolution regime providing HM Treasury, the Bank of England and the appropriate regulator (the authorities) with tools to deal with banks that get into financial difficulties.

The special resolution regime in the Banking Act applies to the following:

- UK incorporated institutions authorised under the Financial Services and Markets Act 2000 to accept deposits (although note that the regime applies in a modified way only to building societies and not to credit unions);
- building societies (although there are specific modifications here);

- systemically important investment firms (these are UK investment firms that have an initial capital requirement of €730,000);
- recognised central counterparties (CCP) (these terms are defined in the legislation but means UK clearing houses and clearing houses whose application for authorisation under Regulation (EU) No. 648/2012 on OTC derivatives, central counterparties and trade repositories have yet to be determined);
- banking group companies (these are certain specified undertakings that are in the same group as a bank, investment firm or CCP; and
- banks that are not regulated by the Prudential Regulation Authority (PRA) (note that this provision is to future-proof the legislation as there are currently no UK banks that are not simultaneously authorised and regulated by the PRA).

The special resolution regime provides for five pre-insolvency stabilisation options: transfer to a private sector purchaser; transfer to a bridge bank; transfer to an asset management vehicle; bail-in and transfer to temporary public sector ownership. In addition, there are two insolvency options (see below). There are seven special resolution objectives which the relevant authorities must have regard to:

- ensuring the continuity of banking services in the UK and of critical functions;
- the protection and enhancement of the stability of the UK financial systems;
- the protection and enhancement of public confidence in the stability of the UK's financial system;
- the protection of public funds;
- the protection of depositors;
- the protection of client assets; and
- the avoidance of interference with property rights in contravention of a human right, in particular article 1 of the First Protocol of the European Convention of Human Rights.

A Code of Practice is in force giving guidance on the use of the special resolution tools.

The two insolvency options that form part of the special resolution regime in the Banking Act are bank insolvency and bank administration. The aim of bank insolvency is to provide for the orderly winding up of a failed bank or financial institution. The provisions are based on existing liquidation provisions. The aim of bank administration is to put into place a bank or financial institution administration procedure to deal with the residual part of a bank or financial institution where there has been a partial transfer of business to a private-sector purchaser or bridge bank pursuant to the special resolution provisions. A bank administrator may be appointed by the court to administer the affairs of the residual part of the insolvent bank.

The Banking Act excludes investment banks from the bank insolvency and administration procedures set out above where the investment bank is not an authorised deposit-taking institution. However, the Banking Act enabled a special regime to be put in place for investment firms. This is set out in the Investment Bank Special Administration Regulations 2011 (SI 2011/245) (the Regulations) and the Investment Bank Special Administration (England and Wales) Rules 2011 (SI 2011/1301). The administrator has three objectives: to ensure the return of client assets (including money) as soon as is reasonably practicable; to ensure timely engagement with market infrastructure bodies and the Bank of England, HM Treasury and the PRA; and to either rescue the investment bank as a going concern or wind it up in the best interests of creditors. The administrator is obliged to commence work on each objective immediately after appointment, but has the flexibility to prioritise the order of work as he or she thinks fit (subject to any PRA direction), in order to achieve the best result overall for clients and creditors. In general, the administration provisions set out in the Insolvency Act apply in the case of a special administration, subject to certain modifications set out in the Regulations. Where the investment bank is also a deposit-taking bank with eligible depositors, the Regulations allow the bank to be put into special administration (bank insolvency) or special administration (bank administration).

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**Secured lending and credit (immoveables)**
**6 What principal types of security are taken on immoveable (real) property?**

The principal type of security granted over immoveable property is the legal mortgage. This is a transfer of the whole of the debtor's legal ownership in the property subject to the security. It is subject to the debtor's right to redeem the legal title upon repayment of the debt (known as the equity of redemption). The appearance of ownership remains with the debtor although the legal mortgage affects an absolute transfer subject to the right of redemption.

An alternative is the equitable mortgage, which creates a charge on the property but does not convey any legal estate or interest to the creditor. It can be created by a written agreement to execute a legal mortgage, by a mortgage of an equitable interest or by a mortgage that fails to comply with the formalities for a legal mortgage.

Another alternative is the fixed charge. This involves no transfer of ownership but gives the creditor the right to have the designated property sold and the proceeds applied to discharge the debt. A fixed charge attaches to the property in question immediately on creation (or, if acquired later, after creation but immediately on the debtor acquiring the rights over the property to be charged). The debtor may then only dispose of the property once the debt has been repaid or with the consent of the creditor.

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**Secured lending and credit (moveables)**
**7 What principal types of security are taken on moveable (personal) property?**

The principal types of security relating to moveable property are mortgages and fixed charges (see question 6), floating charges, pledges and liens.

A floating charge does not attach to a specific asset but is created over a class of assets, present or future, and allows the debtor to buy and sell such assets while the charge remains floating. Floating charges are generally created over the whole business and undertaking of a company. It is only on the happening of a certain event, such as default on the repayment of the debt, that the charge attaches to the secured assets that are at that time owned by the debtor. This is called 'crystallisation'. On crystallisation, the charge acts like a fixed charge in that the debtor is no longer free to sell the assets without repayment of the debt or without the consent of the creditor.

A pledge is a form of security that gives the creditor a possessory right to the pledged asset. It is usually created by delivering the asset to the creditor, although symbolic or constructive delivery may be sufficient.

A lien is a possessory right of a creditor to retain possession of a debtor's asset until the debt has been repaid. It can be created by contract or by operation of law. The creditor has no right to deal with the asset and the lien is usually extinguished once the asset is returned to the debtor.

The Financial Collateral Arrangements (No. 2) Regulations 2003 (the FCA Regulations) are intended to give effect in England and Wales to the European Union Directive 2002/47/EC on financial collateral arrangements (the FCA Directive) in order to create a simple, effective legal framework for the use of securities (financial instruments) and cash as collateral by title transfer or pledge, removing burdensome formalities of execution, registration and enforcement. They also disapply certain provisions of the Insolvency Act. The FCA Regulations only apply to security over cash (including claims for repayment of money), credit claims (loans made available by credit institutions), financial instruments and shares. The FCA Regulations apply to arrangements made on or after 26 December 2003 (the date the FCA Regulations came into force), and case law has confirmed that they do not have retroactive effect. The FCA Directive provides that the security provider and taker must be a public authority, a central bank or other international bank, financial institution or central counterparty, settlement agent, clearing house or similar institution. The FCA Regulations do not contain this element. This has led to doubts about whether the FCA Regulations were valid made under the European Communities Act 1972 (see *The United States of America v Nolan* [2015] UKSC 63).

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**Unsecured credit**
**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to unsecured creditors?**

Certain creditors may have the benefit of a lien imposed by statute over the assets in their possession (see question 7). A supplier of goods may protect himself or herself by inserting a clause in the supply contract to the effect that title to the goods supplied will not pass to the buyer until payment has been received (known as a 'retention of title' or ROT clause). The contract can either provide for retention of title until the specific goods supplied by the contract have been paid for or, more usually, until all monies outstanding from the debtor have been paid. The creditor is therefore contractually entitled to the return of goods.

If none of the above remedies are available, then an unsecured creditor will need to commence proceedings against the debtor for debt recovery. If there is no substantive defence to the claim, the creditor can apply for summary judgment, which could take up to three months. If the debtor can show that he or she has a real prospect of successfully defending the claim, it could take much longer. In the meantime, if the creditor has evidence that the debtor is likely to dissipate his or her assets he or she can apply to the court for an order that assets up to the amount claimed be frozen or prevented from being dealt with or dissipated. Once a judgment has been obtained, then enforcement proceedings can commence. Remedies include sending a court officer to seize the debtor's goods or diverting an income source directly to a creditor (a third-party debt order).

Creditors (including unsecured creditors) can also apply to the court for a winding-up order, proceeding directly with an application for a winding-up order or serving a statutory demand on the debtor first (see question 1). Where a debt is genuinely disputed the dispute should be resolved through the commercial courts – the courts have consistently held that a winding-up petition should not be used as a way to enforce a debt where there is a triable issue. Unsecured creditors are also able to make an application to court for the appointment of administrators (see question 11 below).

There are no special rules for foreign creditors except that they may sometimes be required to provide security for the debtor's legal costs by making a payment into court.

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**Voluntary liquidations**
**9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?**

There are two different procedures for the voluntary liquidation of a company, members' voluntary liquidation (a solvent liquidation) and creditors' voluntary liquidation (typically, an insolvent liquidation).

**Members' voluntary liquidation (MVL)**

If the directors are able to swear a statutory declaration that the company is solvent, a company can be placed into MVL. The MVL is commenced once the shareholders pass a special resolution (75 per cent majority) to place the company into liquidation. The shareholders choose the identity of the liquidator and he or she is appointed by ordinary resolution (over 50 per cent). On the liquidator's appointment, the directors' powers will cease. There is no automatic stay of proceedings once an MVL has commenced and generally, the court is not involved in an MVL. However, the court may order that any particular proceeding is stayed or partially stayed under its general, discretionary power.

If the liquidator subsequently determines that the company is, in fact, insolvent, then the MVL should be converted into a creditors' voluntary liquidation.

**Creditors' voluntary liquidation (CVL)**

If the company is insolvent, or the directors are unable to swear a statutory declaration as to solvency, a company can be placed into a CVL. Like an MVL, the process is started by the shareholders passing a special resolution (75 per cent) resolving to place the company into liquidation. The shareholders will also appoint a liquidator, but until the creditors' decision referred to below has taken place, the powers of that liquidator are limited. The directors must then seek a decision from the creditors within 14 days. Currently, the directors convene a physical creditors' meeting (typically on the same day as the shareholders' meeting), at

which the creditors will be given information on the company (a statement of affairs) and at which the creditors may also appoint a liquidator if a resolution is passed by a majority in value of the creditors present and voting. If the shareholders have previously appointed a liquidator, the creditors' choice of liquidator will prevail. The Insolvency Rules 1986 are in the process of being recast, and significant changes will be made to physical creditors' meetings. The new rules are expected to enter into force in the spring of 2017.

On the liquidator's appointment, the directors' powers will cease. Like in an MVL, there is no automatic moratorium on proceedings against the company. The liquidator or any creditor or shareholder may, however, apply to the court for a stay on any proceedings under their general discretionary power.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

In the case of involuntary liquidation (otherwise known as compulsory liquidation or winding up by the court), the creditor must apply to the court for a winding-up order. The most likely ground for a winding-up order is that the company is unable to pay its debts (see question 1).

If the court makes a winding-up order, the winding up is deemed to commence at the time of the presentation of the winding-up petition rather than at the date of the order (unless the winding-up order is made following an application for administration which the court determines to treat as a winding-up petition, in which case the winding-up is deemed to commence on the making of the order). Any disposition of the company's property and any transfer of shares made after the commencement of the winding up is, unless the court orders otherwise, void.

Once the winding-up order has been made, no action may be started or proceeded with against the company without the court's permission. The directors' powers will also cease at the time of the winding up order. In addition, the business of the company ceases except to the extent necessary for it to be wound up.

A secured creditor holding a qualifying floating charge can, in limited circumstances, appoint an administrative receiver. An administrative receiver realises the secured debt for the benefit of the debenture holder who appoints the administrative receiver. There is no statutory purpose of administrative receivership. Given the non-collective nature of the process, the availability of appointing administrative receivers was significantly curtailed by the Enterprise Act 2002. Following this Act, it is now only possible to appoint an administrative receiver under a qualifying floating charge where it is a charge created before 15 September 2003 or if a charge is created after this date, if it falls within certain exemptions (eg, if there is a capital market arrangement).

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

There are three main processes set out by legislation, which are: company voluntary arrangements; schemes of arrangement; and, to a lesser degree, administrations.

#### Company voluntary arrangements (CVAs)

The process for a CVA is set out in Part 1 of the Insolvency Act. A CVA is an agreement between a company, its shareholders and its (unsecured) creditors where the directors (or a liquidator or administrator) propose a reorganisation plan, which usually involves delayed or reduced debt payments or a capital restructuring.

The CVA commences with the directors making a written proposal to an insolvency practitioner (called the nominee) who files a report with the court on whether to call meetings of the shareholders and creditors of the company to consider the proposal. While the nominee's report is filed at court, there is no court hearing or judicial examination on the matter. If the nominee concludes that the meetings should be held, a meeting of the company's shareholders and a meeting of the company's creditors is called. At the shareholder meeting, the proposal must be approved by 50+ per cent (in value). At the creditors' meeting, the proposal must receive the approval of 75 per cent (in value) of the company's creditors, present and voting. In addition to this requirement, a resolution will be invalid if those creditors voting

against it include more than half in value of the 'unconnected' creditors. The definition of 'connected' is set out in the Insolvency Act and is very broad, most importantly including the company's shareholders. Votes are calculated according to the amount of the creditor's debt as at the date of the meeting.

Where the requisite approvals have been obtained, the CVA will bind every creditor who was entitled to vote at those meetings except for preferential and secured creditors, who are not bound by the CVA unless they agree to be. Where the meeting of shareholders and creditors produce conflicting conclusions, the creditors' decision prevails. However, in this case, a shareholder can within 28 days apply to the court for an order reversing or modifying the creditors' decision. Creditors may also apply to court to challenge the CVA within 28 days of the approval being reported to court if they think that they have been unfairly prejudiced or there has been a material irregularity in the conduct of the meetings. Once the CVA has been approved the nominee becomes the supervisor and is tasked with ensuring that the terms of the CVA are implemented.

During the CVA process there is usually no statutory moratorium. However, a 'small company' (defined by reference to its turnover, balance sheet and number of employees) wishing to propose a CVA can benefit from an initial 28-day moratorium.

CVAs are often used in the context of implementing an operational restructuring of a business (as opposed to a financial restructuring) – not least because of the inability to bind secured creditors in this process.

#### Schemes of arrangement

Schemes of arrangement are governed by the Companies Act 2006 and provide a mechanism enabling a company to enter into a compromise or arrangement with its creditors (including secured creditors). The process is commenced by a court application (ordinarily by the company, but this could also be made by any creditor, a liquidator or administrator) for an order that a creditors' meeting be summoned. At the creditors' meeting, the scheme is approved if 75 per cent in value and the majority in number of each class of creditors present and voting votes in favour. A second court application is then required at which the court is asked to sanction the scheme. Once sanctioned and delivered to the Registrar of Companies, the scheme will be binding on all the company's creditors.

Creditors can challenge the scheme in court at either the hearing for permission to convene the scheme meetings or the hearing to sanction the scheme. The usual grounds for challenge are that the class meetings were improperly constituted, the creditors were not given sufficient information or the scheme is unfair. During the scheme process there is no statutory moratorium. However, the court will generally be supportive of the restructuring process, assuming that the scheme has a reasonable prospect of succeeding. In one case, the court was even prepared to grant a temporary stay of proceedings for summary judgment against a company that is in the process of implementing a scheme (*FMS Wertmanagement AÖR v Vietnam Shipbuilding Industry Group & Ors* [2013] EWHC 1146 (Comm)). Recently, companies have also used a scheme to achieve a standstill period in which to progress a restructuring. Interestingly, these schemes did not implement the actual restructuring but simply provided the means to achieve a moratorium that was not obtainable without cram down of creditors (see the cases of *Metinvest (Re Metinvest BV* [2016] EWHC 79 (Ch)) and *DTEK (Re DTEK Finance BV* [2015] EWHC 1164 (Ch)).

A company is entitled to implement a scheme if it is capable of being wound up in England and Wales. Case law has clarified that a company could be wound up in England and Wales if it could be said to have 'sufficient connection' with England and Wales. The question as to what constitutes 'sufficient connection' is a factual one but recent case law has continually reduced the threshold. A foreign company with either its COMI or an establishment in England has sufficient connection with England. Equally, there are a number of cases where sufficient connection was demonstrated because the facility documents were governed by English law and contained a clause granting exclusive and non-exclusive jurisdiction in favour of the English courts. Cases have included a scheme of arrangement where the facility agreement was not originally governed by English law but where governing law and jurisdiction were amended to English law as part of the restructuring process just before the scheme proposal for the purpose of establishing sufficient connection (*Re Apco Parking Holdings GmbH* [2014]

EWHC 1867 (Ch)) and where a new UK-incorporated company that voluntarily assumed obligations under the debt to be compromised was added to the group in order to be the scheme company (*Re Codere Finance (UK) Ltd* [2015] EWHC 3778 (Ch)). The English courts have therefore taken an expansive view of sufficient connection (even where this is established late and for the purpose of the scheme). Companies will need to take care to ensure that an English law scheme is capable of being enforced in the jurisdiction in which the company's assets are situated. An English law decision is of limited value if creditors are still able to take unilateral action to recover their 'schemed' debts in overseas jurisdictions. Generally, the English courts will require expert evidence that the scheme would be capable of being enforced in the home jurisdiction(s) of the debtor, which usually takes the form of a legal opinion from a legal academic qualified to practise in the relevant area of law. A scheme may also be combined with recognition proceedings in other jurisdictions, for example, Chapter 15 of the US Bankruptcy Code.

Schemes have been used to effect a 'balance sheet restructuring' and are sometimes combined with an administration (particularly where there is a need for a moratorium) or a CVA that can deal with the operational elements of a restructuring.

### Administration

A company can achieve a successful financial reorganisation without the need to enter into any formal insolvency procedure, although if creditors are not generally supportive of the restructuring process or do not have confidence in the company's management it may be necessary to place the company into administration. Administration is an alternative insolvency procedure to liquidation that allows a (normally insolvent) company to continue trading with protection from its creditors by way of a moratorium (see question 15). This may give the company sufficient breathing space to be reorganised and refinanced. While a company is in administration it is controlled by an administrator, who will be a licensed insolvency practitioner, and to all effects and purposes, the directors' powers will cease (although they will remain in office). There is both a court-based procedure (via an administration application) and an out-of-court route (for use by a holder of a qualifying floating charge (QFC) or by the company or its directors) to place a company in administration.

The objectives of an administration are to be achieved via a waterfall effect. The primary objective is to rescue the company as a going concern and only if the administrator thinks that this objective is not reasonably practicable, or that a better result will be achieved for the company's creditors by some other means, can he or she consider the second or third objectives; achieving a better result for the company's creditors as a whole than would be likely if the company were wound up; or realising property to make a distribution to one or more secured or preferential creditors. An administration may last one year only (unless it is renewed with the consent of the creditors for one year, once, or with the consent of the court for an unlimited period of time). The administrator can collect in and distribute the company's assets. An administration can terminate either because the company is dissolved or because the administration is converted into a liquidation.

Note also the UK government consultation 'A review of the corporate insolvency framework' referred to in question 1. If the UK government implements some of the suggested topics of reform, this will impact voluntary reorganisations significantly. In particular, the restructuring moratorium and the flexible restructuring plan will provide a new landscape to implementing voluntary reorganisations. At this stage, it is not yet known whether the UK government will implement some of the reforms, and, if so, how.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Although this is unusual, it is possible for a creditor to propose a scheme (but not a CVA). As a practical matter, a creditor is unlikely to have sufficient information to propose a satisfactory restructuring of the company's affairs.

A creditor may apply for the company to be put into administration and subsequently the administrator may propose either a CVA or a scheme. Where the creditor is a secured creditor holding a QFC,

the appointment of the administrator may be made following a court-based procedure or an out-of-court route. If the creditor is unsecured, it must apply to court for an administration order.

The effects of the commencement of the reorganisation are discussed in question 11.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

There is no express duty to commence insolvency proceedings at any particular time on the grounds of either cash flow or balance sheet insolvency, although directors may commence proceedings to try to minimise the risk of personal liability for wrongful trading.

Under section 214 of the Insolvency Act a liquidator or an administrator can bring an action against directors, former directors and 'shadow directors' for wrongful trading. A director may be held liable where he or she continues to trade after a time when he or she knew, or ought to have concluded, that there was no reasonable prospect of the company avoiding insolvent liquidation or administration. To avoid liability, once there is no reasonable prospect that a company can avoid going into insolvent liquidation or administration, directors must take every step to minimise potential loss to creditors and cannot simply walk away. This may involve filing for an insolvency procedure.

A consequence of carrying on business when insolvent can be that the court finds a director guilty under section 214. The court may declare that person liable to make such contribution to the company's assets as the court thinks proper, the amount being compensatory rather than penal.

It should also be noted that special administrators, appointed under bank administration, building society special administration and investment bank special administration, can also bring an action for wrongful trading under section 214 of the Insolvency Act.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

A reorganisation can, and is typically, implemented outside of any formal insolvency or pre-insolvency procedure. If there is a reasonable prospect that the company will avoid going into insolvent liquidation or administration, the debtor can continue to carry on business during a reorganisation. Note that having this reasonable prospect is not a prerequisite in law to carry on the business. However, in practice directors will be wary about continuing to trade where there is no such reasonable prospect due to wrongful trading concerns (see question 13). They will be focused on ensuring that every step is taken to minimise loss to creditors, which often includes putting in place mechanisms to protect any new liabilities. If there is a consensual restructuring process, the creditors involved may require additional information about the company during this process and increased access to management. Other creditors, for example suppliers, may also change their terms of business to afford greater protection should the reorganisation fail and the company subsequently go into insolvent liquidation or administration. If no formal insolvency proceedings have commenced, creditors who continue to supply goods and services during the reorganisation process will not be subject to a particular statutory regime. Existing contractual arrangements continue to apply. In a reorganisation outside a formal insolvency process, the directors retain their management powers and will be tasked with driving the restructuring.

A reorganisation could also be implemented via an administration of the debtor (or the debtor's holding company). In administration, the administrator can carry on the business of the company where that is consistent with the purpose of the administration. To carry on the business, the administrator will pay creditors who supply goods or services

to the company in administration in priority to ordinary unsecured creditors as expenses of the administration (otherwise the counterparty would not be likely to continue to trade). However, debts that had arisen prior to the insolvency will remain a provable debt and rank *pari passu* with other unsecured creditors. Certain types of supplies are protected by legislation and suppliers are prevented from terminating their supply (regardless of contractual termination rights) where the company is in an insolvency process and the office holder requests the continued supply. As from 1 October 2015, these include public utilities, such as gas and electricity as well as private suppliers of utilities, including supplies from a landlord to a tenant. In addition, communication services by a person whose business includes providing communication services as well as chip and PIN machines, computer hardware and software IT assistance connected to IT use, data storage and processing and website hosting services are 'protected supplies' if the relevant contract was entered into on or after 1 October 2015.

At various stages of the administration, the administrator must report to creditors and seek their approval for his or her proposals for achieving the purpose of the administration. The creditors may also appoint a creditors' committee that will have a supervisory function. An administrator is an officer of the court and may apply to the court for directions on how to conduct the administration. If a creditor believes that the administrator is not conducting the administration properly, that creditor may apply to the court for relief, which could include the removal of the administrator.

Separately, where a creditor has been granted fixed charged security over an asset of the company the administrator will require consent from the relevant fixed charge creditor or the court to release any such assets before such asset can be disposed of and the fixed charge creditor will be entitled to the net proceeds of sale. An administrator is able to deal with (and sell) assets subject to a floating charge without the charge holder's permission.

In a reorganisation outside a formal insolvency process, the directors retain their management powers and will be tasked with driving the restructuring.

If a reorganisation is implemented in the context of a formal insolvency process the directors' powers will depend on the type of process. For example, in administration, once the administrator is appointed, the directors' powers to exercise any management function, or actions that interfere with the administrator's powers, cease unless prior consent is given by the administrator. By contrast, in a CVA the directors remain in control with the assistance and supervision of the nominee and supervisor of the CVA.

Note also the UK government consultation 'A review of the corporate insolvency framework' referred to in question 1. If the UK government implements some of the suggested topics of reform, this will impact how a company in financial difficulties can do business while it undergoes a reorganisation significantly. In particular, the restructuring moratorium, rescue finance plans and designation of certain contracts as essential are likely to have a significant impact.

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## Stays of proceedings and moratoria

### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

#### Liquidations

When a company is placed in compulsory liquidation, no action or proceeding may be started or proceeded with against the company or its property without the court's permission. Permission will be refused if the proposed action raises issues that could be dealt with more conveniently and less expensively in the liquidation proceedings. However, this will not restrict claims made by secured creditors in respect of secured assets.

When a CVL or a MVL is commenced, there is no automatic moratorium on proceedings against the company. The liquidator or any creditor or member may, however, apply to the court for a stay on any proceedings. Such a stay will not be granted automatically, but will usually be granted where proceedings were commenced after the members' resolution (for more details on voluntary liquidations see question 9).

#### Reorganisations

The vast majority of reorganisations take place outside of formal insolvency proceedings. It will be up to the company and its creditors in each case to negotiate a stay where this is required. This will be a purely contractual negotiation. Where a stay is essential and cannot be agreed to contractually it may be possible to combine the reorganisation with an administration which then benefits from the automatic statutory moratorium. This may however not be desired in the context of the overall reorganisation.

Note also the UK government consultation 'A review of the corporate insolvency framework' referred to in question 1. If the UK government implements some of the suggested topics of reform, this will impact the available stays and moratoria in the UK.

If the restructuring is implemented by way of a scheme of arrangement and if it has the support of the majority of creditors and so has a reasonable chance of success, the court has in the past granted a temporary stay of proceedings against the company (see *FMS Wertmanagement AÖR v Vietnam Shipbuilding Industry Group & Ors* [2013] EWHC 1146 (Comm)) and question 11). Recently, companies have also used a scheme of arrangement to achieve a standstill period in which to progress a restructuring. Interestingly, these schemes did not implement the actual restructuring but simply provided the means to achieve a moratorium that was not obtainable without cramdown of creditors (see the cases of *Metinvest (Re Metinvest BV* [2016] EWHC 79 (Ch)) and *DTEK (Re DTEK Finance BV* [2015] EWHC 1164 (Ch)).

Administration can also be used to implement reorganisations (see question 10). An interim moratorium comes into force on the date when an application is made for the appointment of an administrator, or when notice of the intention to appoint an administrator is filed with the court. This interim moratorium is made final once the company has gone into administration. There is little difference in the extent of the temporary and the final moratorium. The moratorium means, among others, the following:

- no steps can be taken to enforce security over the company's property or to repossess goods in the company's possession under any hire-purchase agreement without the consent of the administrator or the court's permission;
- a landlord may not exercise a right of forfeiture by peaceable re-entry in relation to premises let to the company without the consent of the administrator or the court's permission; and
- no legal process (including legal proceedings, execution, distress and diligence) may be instituted or continued against the company or its property without the consent of the administrator or the court's permission. This would include, for example, civil or criminal proceedings or other proceedings of a judicial or quasi-judicial nature.

Broadly speaking, permission will be granted if to do so is unlikely to impede the achievement of the purpose of the administration. The court will engage in a balancing exercise weighing the interests of the individual creditor seeking to lift the moratorium against the interests of the creditor body as a whole.

As an alternative to going into administration, a small company (as defined by section 382 of the Companies Act 2006) may obtain the protection of a 28-day moratorium while it puts together a CVA (see question 11). Many of the features of this moratorium are similar to those that apply while a company is in administration. With creditor consent, the moratorium may be extended by up to two more months.

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## Post-filing credit

### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

A liquidator and an administrator can raise, on the security of the company's assets, any money required. Such credit would have priority over ordinary unsecured creditors as an expense of the insolvency but only in respect of the new funds. Liquidation and administration expenses are also paid out of floating charge realisations in priority to payments to the floating charge holder (see question 33 for further detail).

However, in each case, any new loans and security will not take priority over pre-existing secured debt unless this is permitted under the terms of the pre-existing secured indebtedness and security documents.

In an informal restructuring, or a restructuring implemented by way of a scheme or a CVA, the obtaining of credit and the use of assets as security is a matter for agreement between the company and its creditors and the type of restructuring process implemented. So, for example, security could be released as a consequence of a scheme of arrangement with the support of the requisite majority of creditors, but as a CVA is unable to bind secured creditors without their consent, this would not be possible in a CVA (unless the secured creditor agrees).

Note also the UK government consultation 'A review of the corporate insolvency framework' referred to in question 1. If the UK government implements some of the suggested topics of reform, this may impact the availability of post-filing credit significantly. One of the proposals is to encourage rescue financing, meaning more options than are currently available are likely to be available to companies and lenders. The consultation sets out a number of possibilities to encourage rescue financing.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Prior to the commencement of a formal insolvency procedure, contractual rules on set-off and netting apply. These rules could be amended by agreement as part of an informal reorganisation.

Insolvency set-off applies where there have been mutual dealings between a creditor and the company. The liquidator or administrator is required to take an account of what is due from each party to the other in respect of dealings and set off these sums. Set-off is mandatory, automatic and self-executing. This means that where the test is met, the parties have no choice and their claims are set off as a matter of law – it cannot be contracted out of. The effect of this is that unsecured creditors entitled to set-off have an advantage over other unsecured creditors as they will receive £ for £ rather than a diluted dividend. Note, however, that there are special provisions that apply to certain contracts in the financial markets. Insolvency set-off applies both in a liquidation (from the date that the liquidation takes effect) and in administration (but then only when the administrator has given notice of his or her intention to make a distribution to creditors).

Pursuant to the terms of the FCA Regulations, a close-out netting provision in a security document will apply even if the collateral provider or collateral taker is subject to winding-up proceedings or reorganisation measures, unless at the time the arrangement was entered into or the relevant financial obligations came into existence the other party was or should have been aware of such winding up or reorganisation.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

##### Reorganisations

In practice, many reorganisations result from negotiations with creditors outside of any formal insolvency or restructuring procedures. Consequently, the terms of the reorganisation and therefore any provisions as to the sale or use of assets are subject to negotiation between all relevant parties and will be documented by way of contract.

##### Liquidations

Once a company has entered liquidation, the liquidator can sell any of the company's property by public auction or private contract, provided the assets are beneficially owned by the company (see question 3). This power can be exercised in both voluntary and compulsory liquidations without sanction of the court or liquidation committee. A liquidator can sell assets that are subject to floating charge security as if the charge did not exist but will need the consent of a holder of fixed charge security in order to sell this. Where such consent

is obtained it will be a matter for negotiation as to whether the asset is sold free and clear of the security (with the liquidator accounting to the secured creditor for the purchase price) or whether the asset will be transferred subject to the security (which in many cases will not be satisfactory to a purchaser). Where a liquidator sells part or all of a business in liquidation, there is an exemption to the Transfer of Undertakings (Protection of Employment) Regulations 2006 (TUPE), which specifies that any dismissals by reason of the transfer will not automatically be unfair. This is in contrast to a sale in administration (see below).

##### Administrations

If a reorganisation occurs in the context of an administration, the administrator can carry on the business of the company to sell its assets, including secured or leased assets, where the disposal would be likely to promote the purposes of the administration. Where the assets are leased, subject to a valid ROT clause or are secured by a fixed (as opposed to a floating) charge, court sanction is required before an administrator can sell the assets without the lessor's or chargee's consent. Where the entire business (or a line of business) is sold by the administrator a tool called 'pre-pack administration' is often used. A pre-pack is in essence a sale of the business or assets of an insolvent company by an administrator where all the preparatory work for the sale (ie, identifying the purchaser, negotiating the terms of the sale and valuing the assets (potentially but not always via a marketing process)) takes place before the appointment of the administrator and the sale is then concluded immediately after his or her appointment. Where an administrator sells part or all of a business in administration, he or she must have regard to TUPE, which stipulates that certain employment contracts will automatically transfer to the purchaser.

To ensure transparency in respect of pre-pack sales, the Joint Insolvency Committee published Statement of Insolvency Practice (SIP) 16. This gives guidelines to insolvency practitioners regarding disclosure in the context of pre-pack sales, and requires office holders to submit a SIP16 statement to creditors following any pre-pack undertaken. It is important that creditors are provided with a detailed explanation and justification of why a pre-packaged sale was undertaken and details of any marketing process and valuations obtained (or an explanation of why no marketing or valuations were undertaken), so that they can be satisfied that the administrator has acted with due regard for their interest. Where a sale is to a connected party, the potential purchaser is encouraged to submit details of the proposed acquisition to a 'prepack pool' (a panel of insolvency experts). The pre-pack pool is to provide an opinion on the sale.

Although SIP16 is not legally binding, failure to comply could result in an administrator facing disciplinary action from his or her professional body.

##### 'Stalking horse' bids and credit bidding

There is no specific legislation that either prevents or encourages the use of 'stalking horse' bids in sale procedures. How a particular sale process is carried out will be at the discretion of the directors or insolvency practitioner (as applicable), but regard needs to be had to the duties owed to creditors, and procedural guidance such as SIP16 (referred to above).

Credit bidding (including where the credit bidder is the assignee of the original creditor) in sales is permitted, although there is also no specific legislation on this point. The sale will not necessarily be the subject matter of a court decision, indeed in most cases it will be up to the insolvency office holder to decide whether a particular deal is in the best interest of the creditors and so should be implemented.

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

There is no automatic right of a licensor or owner of IP to terminate the debtor's right to use IP assets. Such matters will be governed by the

terms of the licence, for example, in particular in the event of default and termination provisions. Where the contractual provisions permit a termination, then this will be permitted under English insolvency law unless the supply is a protected supply (see question 13) in which case the supplier's ability to terminate the contract or the supply will be severally restricted. Note also the UK government consultation 'A review of the corporate insolvency framework' referred to in question 1. An insolvency representative does not have power to terminate a debtor's agreement with an IP licensor or owner and then continue to use the IP for the benefit of the estate.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

A data controller is required to comply with the data protection principles set out in the Data Protection Act (the DPA) when processing any personal data. The first such data protection principle is that personal data must be processed fairly and lawfully. Where valuable customer data is collected by the insolvent company, it is one of the assets that an insolvency office holder is able to realise for the benefit of creditors. The DPA applies, and it is usual for an office holder to require a buyer of the data to comply with all the seller's obligations under the DPA and to provide an indemnity to the seller and the office holder against any liability for failure to have complied. This is often supported by an agreed form 'fair processing' notice, which the buyer will be required to send to each customer to inform the customer that the buyer is now the data controller and of any new purposes for which the customer's personal data will be processed by the buyer. Guidance from the Information Commissioner's Office takes the view that, in the case of insolvency, a customer database can be sold without obtaining the customers' prior consent; however, if the buyer wants to use the information for a new purpose, the buyer will need to get consent from each customer.

In *Re Southern Pacific Personal Loans* [2014] Ch 426, the English court held that liquidators do not constitute data controllers in their own right and are not personally responsible for the company's compliance with the provisions of the DPA. The liquidators instead act as agents for the company in taking decisions on its behalf. The liquidators in that case were concerned that the insolvent company should not be required to continue to hold personal data in order to comply with data access requests made by former customers. The court agreed that, in principle, personal data should be destroyed as soon as possible after the company ceases to conduct business, provided that the company must retain sufficient data to comply with any outstanding data access requests made before the data are destroyed. The court further qualified the principle by saying that liquidators must ensure that the company retains sufficient data to enable them to deal with any claims that may be made in the liquidation. The court held that in circumstances in which the liquidators had reason to anticipate the possibility of claims, they would be required to advertise for claims against the company and allow sufficient time for responses before disposing of personal data.

### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

In a reorganisation outside a formal insolvency process, the debtor has no legal right to reject or disclaim an unfavourable contract.

#### Administration

An administrator does not ordinarily have the power to disclaim onerous property. The exception to this is that special administrators, appointed under bank administration, building society special administration and investment bank special administration, can disclaim onerous property. As a matter of law, administration does not terminate contracts entered into by the company. Any termination provision must be expressly set out in the contract. In practice, the administrator may choose not to comply with contracts entered into by the company

prior to administration. An administrator may, for example, decide that the return for creditors is higher if a particular contract is not complied with rather than if the contract continues to be complied with. This is – as for a solvent company – a pure commercial decision where the administrator will consider his or her duties to the creditors as a whole. Where an administrator has breached a contract that existed prior to the insolvency, any damages for breach will rank as a provable debt. Where an administrator breaches a contract entered into by him or her after the insolvency, damages for breach will rank as an expense of the administration and will therefore have 'super priority' (ie, be paid ahead of holders of floating charge security and unsecured creditors).

#### Liquidation

Liquidation is not a reorganisation procedure but could be used following reorganisation if assets of the company have been sold. It is (other than special administration regimes) the only process in which an unfavourable contract can be disclaimed. A liquidator may disclaim any onerous property. Onerous property is defined as any unprofitable contract, and any other company property that is unsaleable, is not readily saleable or is such that it may give rise to a liability to pay money or perform any other onerous act. Property is broadly defined and it includes money, goods, things in action, land and every description of property wherever situated and also obligations and every description of interest whether present or future or vested or contingent, arising out of, or incidental to, property. A contract may be unprofitable if it gives rise to prospective liabilities and imposes continuing financial obligations on the company that may be detrimental to the creditors. But a contract is not unprofitable merely because it is financially disadvantageous; it is the nature and cause of the disadvantage that will be the determining factor.

The liquidator cannot disclaim a completed contract. This is because if the company has fully performed a contract then it will have no prospective liabilities, which means that the contract is not onerous and therefore cannot be disclaimed. In addition, there are various specific types of contract in relation to financial markets that the liquidator cannot disclaim.

Further, in the context of property, a liquidator must disclaim the whole of a property (ie, he or she cannot disclaim some and keep the remainder).

The liquidator is not entitled to use his or her power of disclaimer to disturb accrued rights and liabilities – the disclaimer only terminates the contract as to liabilities accruing after the time of the disclaimer.

A disclaimer does not affect transfers of property to the company if, for example, the company bought property that is unsaleable. A disclaimer by the liquidator will not terminate or rescind the sale contract to re-vest the property in the vendor. Its sole effect, in the absence of any other interest in the property, is to vest ownership in the Crown as bona vacantia.

The liquidator can disclaim a contract by notice if it is unprofitable, or simply decline to procure its performance by the company. If the liquidator declines performance then (in addition to other contractual remedies the counterparty may have) it can apply for rescission of the contract and claim for any damages that may be awarded. In either case, the contract comes to an end and the solvent party is left to prove damages for the loss resulting from the company's breach of contract, against which the company can set off the value of the other party's future performance that it has been denied. No time limit is laid down for the exercise of the power of disclaimer. However, a counterparty can require a liquidator to decide whether he or she is going to disclaim or not. If the liquidator then does not give notice of disclaimer within 28 days, he or she loses the right to disclaim.

A disclaimer operates so as to determine, as from the date of the disclaimer, the rights, interests and liabilities of the company, but does not affect the rights or liabilities of any other person except so far as is necessary for the purpose of releasing the company from any liability. A party aggrieved by a disclaimer can apply to the court to reverse the liquidator's decision but the court will not interfere unless the liquidator's action was in bad faith or perverse. Any person suffering loss or damage in consequence of the operation of the disclaimer is deemed to be a creditor of the company and may prove for the loss or damage in the liquidation.

As regards a breach of a contract (which has not been disclaimed), the counterparty will have a claim for breach of contract and will

be able to prove for damages in the liquidation. Where a liquidator breaches a contract entered into by him or her after the insolvency, damages for breach will rank as an expense of the liquidation and will therefore have 'super priority', namely, be paid ahead of holders of floating charge security and unsecured creditors.

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#### Arbitration processes in insolvency cases

##### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

When a company is in administration, the statutory moratorium will apply and will prevent any legal process from being initiated or continued (see question 15). Similarly, in a compulsory liquidation a moratorium is in place. The courts have held that arbitration is a legal process and therefore caught by the moratorium. Arbitration of disputes that arise post-administration would be subject to the same rules (see question 14) as regards whether the administrator or the courts would lift the moratorium to allow the arbitration to progress. However, where the office holder seeks directions from the court (ie, initiates litigation himself or herself, for example, in relation to a set off right) the counterparty will be able to rely on the arbitration clause and force the office holder to arbitrate the claim instead of litigating (see *Philpott & Orton (as joint liquidators of WGL Realisations 2010 Limited)* [2015] EWHC 1065 (Ch)).

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#### Successful reorganisations

##### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

There are no mandatory features in an informal reorganisation; it is a matter for agreement between the creditors.

#### Scheme of arrangement

In a scheme (see question 11), there are also no mandatory features of the reorganisation plan. However, the scheme will need to be better than its alternative (most commonly an insolvency filing but a solvent comparator is also possible). For example, where the alternative to the scheme is liquidation, the scheme must offer a better result for creditors than they would receive in liquidation and evidence must be provided to demonstrate this. The legislation sets out that an explanatory memorandum to a scheme must explain the effect of the compromise or arrangement and state any material interest of the directors and the effect of that interest of the compromise or arrangement.

The process is commenced by a court application, by either the company or any creditor (or, where relevant, the liquidator or administrator), for an order that a meeting of creditors be summoned. There are separate creditors' meetings for each class of creditors. It is the responsibility of the party proposing the scheme to determine the correct classes. If incorrect class meetings are held, then the court will not have the jurisdiction to sanction the scheme.

The classic test for determining the constitution of classes is that a class should comprise 'those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest'. The test for who forms a class is determined in accordance with the creditors' rights under the scheme, as opposed to broader collateral interests. Whether a group of creditors form a single class depends on the analysis of:

- the rights that are to be released or varied under the scheme; and
- any rights that the scheme gives, by way of compromise or arrangement, to those whose rights are to be released or varied.

In many cases, it is not possible to be certain that a particular type of claim constitutes a class of creditors. However, in certain cases the distinction is relatively clear-cut; for example, secured creditors and unsecured creditors will almost certainly constitute separate classes. When an insolvent company proposes a scheme the court will look at the 'insolvency comparator', that is, the rights that the creditors would

have against the company in an insolvent liquidation. The rights of creditors under a scheme can differ from the rights a creditor would have if the company went into insolvent liquidation; indeed, the purpose of many schemes is to produce an arrangement that differs from an insolvent liquidation. However, depending on the differences, this may have an impact on the analysis of which creditors form a separate class for the purposes of the scheme meeting and whether the scheme is fair and should be sanctioned. If the differences apply equally to all creditors, no question of separate classes arises. If the differences produce a result that affects one group of creditors differently from another then, subject to questions of materiality, they should form separate classes.

In order for any proposed compromise or arrangement put forward under a scheme to become binding on the creditors it must be approved by 75 per cent in value and the majority in number of each class of creditors present and voting, and then sanctioned by the court. The scheme will not be sanctioned unless it is fair – that is, a scheme that an intelligent and honest person, a member of the class concerned, and acting in respect of his or her interest might reasonably approve.

A scheme of arrangement can release non-debtor parties. The extent to which a scheme is capable of affecting third-party obligations depends on the extent to which those obligations can be treated as closely connected or ancillary to the company's own obligations and whether those obligations are personal only and not proprietary. The court has confirmed (see *Re La Seda de Barcelona* [2010] EWHC 1364 (Ch)) that, in the case of an English scheme of arrangement, guarantors that are themselves not bound by the scheme of arrangement can have their guarantees released under the terms of the scheme.

#### Company voluntary arrangement

In a CVA there are also no mandatory features (although again the legislation, the Insolvency Rules, sets out the matters that need to be dealt with in the proposal). Note that again, the CVA proposal must lead to a better outcome for creditors than its alternative (most commonly an administration or liquidation). There are no separate classes of creditors in a CVA, although secured and preferential creditors cannot be compromised without their consent. The process for implementing a CVA is set out at question 11. No court sanction is required. On application by a creditor, member or contributory the court may revoke or suspend a CVA that unfairly prejudices the interests of a creditor, member or contributory of a company.

#### Potential new flexible reorganisation plan

Under the UK government consultation 'A review of the corporate insolvency framework' referred to in question 1, a flexible restructuring plan is to be introduced. This may impact how successful reorganisations get implemented in future. At this stage, it is not yet known whether the UK government will implement some of the reforms, and, if so, how.

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#### Expedited reorganisations

##### 24 Do procedures exist for expedited reorganisations?

There are no provisions for the expedition of CVAs or schemes, and the implementation time will depend on its complexity, although the majority of the time spent on the reorganisation is in negotiation with the creditors and in preparation of the settlement documentation. In relation to schemes, which are court-driven processes, the court has been willing to hear applications on an expedited basis and also to convene meetings following comparatively short notice periods where there is an urgent requirement to do so. If a reorganisation is implemented through an administration process, this can be done on a quick timescale using the 'pre-pack administration' tool (set out at question 18).

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#### Unsuccessful reorganisations

##### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A dissenting creditor can defeat a reorganisation that takes place outside of a formal process by refusing to take part or, where appropriate, by applying for the company's liquidation (although the court has to exercise its discretion when making a winding-up order). The

consequences of a breach by the debtor of any contractual agreement will depend on the terms of the agreement but will usually result in the creditor having all his or her previous rights restored.

A proposed CVA or scheme can be defeated if it does not get the statutory majorities of creditors voting in favour of it (see question 11). Assuming that the requisite majorities vote in favour at the scheme meeting, a scheme will be defeated if the court refuses to sanction the scheme either because it does not have the jurisdiction to sanction it, for example because the classes are incorrectly constituted, or because it is unfair. A CVA will be defeated if a creditor, member or contributor brings a successful challenge on the grounds of unfair prejudice or material irregularity at the meetings. A CVA may also be defeated if there is a mismatch between the decisions taken at the creditors' and the shareholders' meetings, and a shareholder successfully applies to court to challenge the decision taken at the creditors' meeting. If a scheme or a CVA is defeated, then unless new restructuring proposals can be agreed with the requisite majorities of creditors, it is likely that the company will be placed in administration or liquidation.

If there is default by the debtor in performing an approved plan in a scheme, the consequences will usually be set out in the scheme. Where there is a material default by the debtor in performing the terms of the CVA, the supervisor of the CVA is likely to issue a certificate of non-compliance setting out the manner in which the company has defaulted and the steps that the supervisor proposes to take. These steps will normally be set out in the CVA.

### Insolvency processes

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

#### Notice, meetings and information and reporting obligations

The Insolvency Rules 1986 set out much of the process relating to each insolvency procedure. The Insolvency Rules are in the process of being recast. The recast is expected to enter into force in spring 2017. At the date of writing, the draft rules have been published but have not been laid before Parliament, so are still subject to change. The recast Insolvency Rules are not intended to be a complete overhaul of existing procedure but do provide for significant changes as regards creditor meetings. Physical creditor meetings are intended to be virtually abolished and one of a number of different types of 'qualifying decision procedure' (eg, deemed decision making) is to be used. Generally, whether it be an administrative receivership or an administration, a compulsory liquidation or a CVL, the Insolvency Act provides for early notification of all creditors by advertisement and for creditors to make decisions.

An administrative receiver must notify creditors following appointment and currently, unless the court directs otherwise, convene a meeting of unsecured creditors within three months of appointment to report on the conduct of the administrative receivership.

Administrators must also notify creditors following their appointment. Currently, a first meeting in an administration must be held as soon as reasonably practicable and within 10 weeks of the administration appointment. The purpose of this meeting is to consider the proposals for the company prepared by the administrator, which must be sent to creditors and members as soon as reasonably practicable and in any event within eight weeks of the administrator's appointment. The administrator is required to send a progress report to the creditors, the courts and the registrar of companies every six months.

In a compulsory liquidation, the official receiver is automatically appointed as liquidator. The official receiver must advertise his appointment. The official receiver may, and if one quarter in value of the company's creditors request it shall, call a creditors' meeting to choose a person to be appointed as liquidator instead of the official receiver. If the liquidator in a compulsory liquidation is not the official receiver, the liquidator must call a final creditors' meeting before the company is dissolved.

In a CVL, currently, a first creditors' meeting will take place shortly after the shareholders pass a resolution to place the company in liquidation. In practice, the creditors' meeting is likely to be on the same

day as the shareholders' meeting. At this meeting, the main purposes will be to appoint a liquidator, fix the liquidator's remuneration and potentially appoint a liquidation committee. The liquidator must call a further creditors' meeting generally if the liquidation lasts more than one year.

### Proceedings against third parties

Since the relevant section of the SBEEA came into force on 1 October 2015, a liquidator or administrator can assign certain causes of action (eg, an action for fraudulent or wrongful trading). The proceeds of the claim or assignment are not to be treated as part of the company's net property, that is to say the amount of its property that would be available for the satisfaction of claims of holders of debentures secured by a floating charge created by the company. In addition, in liquidation any office holder creditor has the right under section 212 of the Insolvency Act to bring proceedings against any company officer or anyone involved in the promotion, formation or management of the company, in relation to the return of any money or property of the company or in connection with any alleged misfeasance or breach of fiduciary duty. Further, a 'victim' of a transaction defrauding creditors may commence proceedings under section 423 of the Insolvency Act.

### Enforcement of estate's rights

**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

Creditors may determine that it is in their best interests to fund the estate or office holder in order that a claim may be pursued by the office holder. Any fruits of the remedies will belong to the insolvency estate.

An insolvency office holder may also assign claims comprised in the company's property at the date of the insolvency and proceedings which are already ongoing at the date of the insolvency. Where such a claim is assigned, the fruits of the remedies can also be assigned. As stated in question 26, since 1 October 2015 an office holder will be able to assign a claim that he or she is entitled to pursue by virtue of being an office holder. These include transaction avoidance claims and wrongful trading claims. Creditors may take action themselves in the limited circumstances described in question 26.

### Creditor representation

**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

In restructurings outside of a formal insolvency process, traditionally the lenders have formed coordinating committees. These creditors usually consist of the largest, or the most influential, creditors. Any appointment is a matter of contract between the lenders and the company (who ordinarily will pay the lenders a fee for their acceptance to be on the coordinating committee and meet the costs of their advisers). More recently, there has been a shift from establishing formal coordination committees to creating more groups of ad hoc lender committees to drive a restructuring.

In a formal insolvency process (such as administration and liquidation), creditors' committees can be formed. A creditors' committee usually consists of between three and five creditors that have been voted into the committee by the creditors. However, the role of the creditors' committee varies taking into account the different natures of these insolvency procedures.

If a liquidation committee is appointed in either a CVL or a compulsory liquidation its role is mainly supervisory and to fix the liquidator's remuneration. The liquidator has to report to the liquidation committee on a regular basis.

The role of a creditors' committee in an administration is substantially the same as in liquidation.

The creditors' committee in an administrative receivership (see question 44) does not have a supervisory role. However, the administrative receiver must provide certain information to the creditors' committee.

Creditors' committees appointed under the terms of the Insolvency Act are not permitted to retain advisers. For creditors' committees

formed by way of contract in restructurings outside of formal insolvency processes the matter will be dealt with contractually.

### Insolvency of corporate groups

**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

English law treats each member of a corporate group as a distinct entity from any of its members, other than in very specific circumstances. Accordingly, the assets and liabilities of companies are not combined into one pool for distribution in an insolvency process. As a practical matter, where there is a corporate group, there may be administrative advantages to having the same insolvency office holder appointed in respect of each of the companies in the group (subject to any conflicts) but each entity will still be treated as separate.

Assets would only properly transfer to insolvency in another country where the office holder determined that the asset did not form part of the company's property. Given the administrator's duty to ensure the best return to creditors, they would not consent to the transfer of such assets without incontrovertible evidence that this was the case or there was a sale of the assets for value.

Under reforms to the EC Regulation on Insolvency Proceedings 2000 (Council Regulation (EC) No. 1346/2000) (the Recast Regulation) a new mechanism is introduced for a group coordination plan. For further detail on the Recast Regulation, refer to the chapter on the European Union.

### Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

Appeals in insolvency proceedings follow the ordinary course for appeals in England and Wales. Appeals of decisions made by a High Court judge will lie to the Civil Division of the Court of Appeal. A decision of the Court of Appeal can be appealed to the Supreme Court, the highest court in the UK. There is no general obligation to post security to proceed with an appeal unless a party specifically applies for the court to order security for costs.

### Claims

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

Generally, unsecured creditors' claims are not submitted until the company is in liquidation. Claims can also be submitted to the administrator, although court approval will be required before an administrator can make a distribution to unsecured creditors (unless it is a distribution from the prescribed part). All creditors submit a claim by sending particulars of it to the liquidator (or administrator) by way of a 'proof of debt'. A creditor may make a claim in respect of a contingent or unliquidated amount provided that it arises prior to the date on which the company went into administration or liquidation or it arises from an obligation to which the company may become subject after the insolvency by reason of any obligation incurred before the company entered liquidation or administration. Interest that accrued prior to the insolvency date can form part of the amount of the creditors' provable debt.

Time limits may be set for receipt and processing of claims before interim dividends are paid. If the creditor misses the deadline he or she will be entitled to receive previous interim dividends (so as to 'catch up') once he or she has proved his claim. Once the office holder has realised all the company's assets he or she will give notice of his or her intention to declare a final dividend.

The liquidator (or administrator) may reject a proof in whole or in part but must provide reasons to the creditors. A creditor may appeal to the court against a rejection within 21 days of receiving notice of it.

### Claims trading

There are no specific provisions dealing with the purchase, sale or transfer of claims against the debtor and no prescribed forms for notifying the insolvency office holder of the trade. If a third party acquires a claim at a discount it will be able to prove for the face value of the claim (the discount is simply a matter between the creditor selling the claim and the acquirer). However, a creditor will not be able to circumvent the automatic and self-executing rules on insolvency set off once it is triggered. Therefore, where set off applies (see question 17), a party will only be able to sell its net balance. In large and complex insolvencies, such as *MF Global*, the office holder may propose a protocol for notifying him or her of trades.

### Interest

Interest that accrued from the insolvency date can be claimed – but is highly subordinated. Once a company in liquidation or administration has paid all provable debts in full, the Insolvency Act provides that creditors with provable debts are eligible to receive interest on those debts for the period from the start of the insolvency process to the date the debt was paid. The current rate of statutory interest is either 8 per cent per annum or the interest rate applicable under the original contract, the greater amount prevailing.

### Modifying creditors' rights

**32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

The court does not have general jurisdiction to change the priority of creditors' claims, which are determined by statute. However, where realisations are made from assets subject to a floating charge, an insolvency office holder must set aside a percentage of such realisations (known as the prescribed part) for distribution to unsecured creditors who would otherwise have ranked in priority below the holder of the floating charge.

Rule 4.218 of the Insolvency Rules sets out a list of winding-up expenses and payment priority. Pursuant to section 156 of the Insolvency Act, the court may, in the event of the assets being insufficient to satisfy the liabilities, make an order as to the payment out of the assets of the expenses incurred in the liquidation in such order of priority as the court thinks just. However, the court's power only extends to being able to vary the order of priority of the winding-up expenses set out in the aforementioned list. Rule 2.67 sets out similar provisions governing expenses incurred in an administration.

### Priority claims

**33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

An office holder will apply the proceeds of the realised assets and pay creditors in a specified order depending upon the source of the proceeds, that is, whether they come from fixed charge realisations, floating charge realisations or the realisations of uncharged assets.

Other than the costs of preserving and realising the fixed charge assets (including the office holder's costs relating to those assets), there are no priority claims that rank ahead of secured creditors with a fixed charge in relation to the proceeds of sale of those assets.

Certain priority claims rank ahead of floating charge holders and these are paid out of the proceeds of sale of the assets secured by the floating charge. These priority claims are preferential debts and payments to unsecured creditors out of the 'prescribed part'. Preferential debts are now split into two categories, ordinary preferential debts and secondary preferential debts. Ordinary preferential debts include sums owed to the occupational pension schemes in respect of unpaid contributions and remuneration owed to employees to a set amount. Where relevant, they also include bank and building society deposits that are covered by the Financial Services Compensation Scheme (FSCS). Secondary preferential debts consist of the part of deposits that are not eligible for FSCS protection either because they exceed the cover level

or because they were made through a branch of an (otherwise) eligible credit institution located outside the EEA. Ordinary preferential debts rank equally amongst themselves before secondary preferential debts which also rank equally amongst themselves. Debts due to the government do not form part of the categories of preferential debts.

The 'prescribed part' is an amount ring-fenced from the company's net floating charge proceeds (up to a maximum of £600,000), which applies when a floating charge was granted after 15 September 2003. This prescribed part is available to unsecured creditors. Case law has clarified that a floating charge holder cannot participate in the prescribed part as an unsecured creditor regarding any shortfall under its floating charge, as this would effectively deprive the unsecured creditors of a substantial part of their already capped benefit. The only way in which a secured creditor could participate in the prescribed part is by releasing its security.

An administrator, liquidator or receiver may apply for an order that the cost of making a distribution to unsecured creditors would be disproportionate to the benefits. However, the court will only grant such order in exceptional circumstances.

The costs and expenses of the liquidator or administrator are paid out of assets subject to a floating charge (so far as the assets of the company are insufficient), taking priority over the claims of the floating charge holder.

Creditors who can establish valid retention of title and other proprietary claims (such as where they are beneficiaries under a trust) rank outside the order of insolvency claims and will, where possible and in accordance with certain legal rules, have their property (or its monetary equivalent) returned to the extent this is still possible.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

##### Reorganisation

In a reorganisation outside of formal insolvency proceedings, normal rules applicable to employment and the termination of employment contracts apply.

##### Liquidation

In a compulsory liquidation, contracts of employment will automatically terminate. Dismissals which take effect on the making of a winding-up order by a court involve a breach of contract by the company for which the employee is entitled to claim damages, effectively by means of a proof of debt in the liquidation.

In a voluntary liquidation, the entry by the employer into liquidation does not automatically terminate the contracts of employment. Given that a liquidator only has limited powers to carry on the business of a company, it is likely that employment contracts will be terminated. An employee may have a contractual claim (eg, for wrongful dismissal) and a statutory right to claim for redundancy or unfair dismissal. In practice, any dismissal or termination of employment contract in an insolvency situation is most likely to be by reason of redundancy and hence for a potentially fair reason under employment legislation. Claims for unfair dismissal or redundancy will rank as ordinary unsecured claims in the insolvency.

##### Administration

Administration does not automatically terminate employment contracts as a matter of law. Following appointment, administrators have 14 days to decide whether to continue to employ individual employees. Failure to take positive action to dismiss will result in the automatic 'adoption' of employment contracts after the expiry of the 14-day period and employees are then entitled to be paid 'qualifying liabilities' which include salary, holiday pay, sick pay, payments in lieu of holiday and contributions to occupational pension schemes. Qualifying liabilities are administration expenses and payable in priority to the administrator's remuneration.

Where contracts of employment are not adopted (and hence terminated), employee claims will generally rank as unsecured claims in the administration, save that employees retain a preferential claim in respect of unpaid wages owed for the four-month period prior to the date of administration, capped at £800. Insolvency office holders will

have liability for all employee PAYE and National Insurance contributions from the date of appointment.

When an administrator sells part or all of a business in administration, he or she must have regard to the TUPE, which will dictate which of the employees is entitled to automatically transfer to the purchaser of the business, such that the employee's contract continues as if the new purchaser were the original employer. If a relevant employees' contract is terminated, both the purchaser or the seller company (in administration) could be potentially liable for all resulting employment claims.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Certain limited unpaid contributions into occupational pension schemes and contributions deducted from the employee's pay are categorised as preferential debts and will rank ahead of floating charge holders in the event of a company's insolvency. Where there is an occupational pension scheme and the employer company enters a formal insolvency process (eg, liquidation, administration or administrative receivership) and there is a deficiency in the scheme, then a section 75 debt (named after section 75 of the Pensions Act 1995) is triggered immediately prior to the employer's insolvency. The section 75 debt is designed to provide a simple debt obligation on an employer and ranks as an ordinary unsecured debt in the employer's insolvency.

If an administrator adopts any employment contracts (see question 34), liabilities under those contracts incurred after adoption will be paid as an administration expense. Such liabilities include contributions to occupational pension schemes.

The Pension Protection Fund (PPF) provides compensation for defined benefit occupational pension scheme members on an employer's insolvency. The Pensions Regulator has 'moral hazard' or 'anti-avoidance' powers to make third parties liable to provide support or funding to a defined benefit occupational pension scheme in certain circumstances. The Pensions Regulator is able to issue a contribution notice to an employer, or a person associated or connected with the employer. If transactions or reorganisations are structured for the purpose of avoiding or, other than in good faith, reducing pension liabilities, those involved are potentially at risk of being required to make a contribution into the scheme equal to the debt that would otherwise have been payable. The Pensions Regulator can also issue a financial support direction (FSD), which requires a party to put in place financial support (broadly, funding or guarantees) and maintain the financial support throughout the life of the scheme. FSDs may be issued against the participating employers or certain parties that are 'connected' or 'associated' with the employer. A party might be at risk of an FSD if the employer participating in the scheme was a service company (ie, a company with accounts showing its turnover principally derived from providing services to other group companies) or it was insufficiently resourced (did not have sufficient assets to meet a prescribed percentage of the debt in relation to the scheme, and at that time there was a connected or associated person who did have sufficient resources). The rules governing who can be associated or connected with an employer are very complex, but generally all wholly owned companies in a group are associated, and significant shareholders (over one-third) will have control and so be associated with the company and its subsidiaries.

In *Bloom v The Pension Regulator* [2013] UKSC 52, the Supreme Court held that an FSD issued against a company that is already in administration was a provable debt as essentially, the relevant facts making the company susceptible to becoming the target of such direction had arisen prior to the insolvency and was thus consistent with the underlying regime imposing the liability.

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Liability for environmental problems in insolvency proceedings can be found under criminal liability, civil liability and administrative liability

(ie, to 'clean up'). There is a plethora of legislation both at the domestic level and derived from European Union legislation that sets out environmental duties and responsibilities and deals with breaches of such duties. The three significant areas of environmental protection in the UK are: (i) the contaminated land regime (with the Environmental Protection Act 1990); (ii) the environmental permitting regime (with the Environmental Permitting (England and Wales) Regulations 2010); and (iii) the water pollution regime (with the Water Resources Act 1991). A company's environmental liabilities (including health and safety related liabilities) will continue regardless of whether the company is solvent or in an insolvency process.

A debtor's officers and directors are liable for the full range of environmental legislation that governs the respective debtor's business. Depending on the legislation, liability can attach to the debtor company and to directors and officers personally. Generally, the prosecutor would need to prove that the individual director or officer knowingly caused or permitted the offence.

Ordinarily, insolvency office holders should not incur liability for offences or torts committed by the debtor prior to the insolvency and any fines, etc, issued prior to the insolvency would rank as an unsecured debt. Following the insolvency, the office holder will be acting in a management role similar to that of directors and will be subject to the duties (and potential liabilities) which go with that role. One potential risk for an office holder is to be required to clean up contaminated land. Should fines or clean-up costs be imposed when a company is in insolvency such costs may still rank as a provable debt (if they can be attributed to steps taken prior to the insolvency). Alternatively, such costs could rank as expenses of the insolvency if they are attributable to something done during the period after insolvency. This will be a matter of fact in each case. Whether an insolvency office holder would be held personally responsible will depend on the particular statute under which the offence is committed and the office holder's conduct. For example, the Environmental Protection Act 1990, dealing with contaminated land, includes a specific protection for insolvency office holders and specifies that no personal liability will attach to them for remedial costs unless a substance was present on the contaminated land as a result of any act done or omission made by the office holder that it was unreasonable for a person acting in that capacity to do or make. This exclusion is, however, not set out as regards other forms of liability (not in relation to contaminated land) where office holders could therefore in theory still be at risk of personal liability.

A liquidator can disclaim onerous property (see question 21) and therefore will be able to disclaim contaminated land and therefore avoid liability following the disclaimer becoming effective.

A secured creditor could become liable for environmental issues if it enforces a mortgage and becomes a mortgagee in possession. Under environmental legislation, a mortgagee in possession is an 'owner' and therefore liability could attach. In relation to an unsecured creditor, it is difficult to see how he or she could become liable (unless he or she acts in a different capacity to that of unsecured creditor).

A third party may be liable for environmental liabilities where for example it caused the environmental damage following the principle that the polluter pays.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Where a debtor uses a CVA or a scheme to reorganise, the terms of the CVA or scheme will determine the treatment of the debtor's liabilities (eg, the extent to which they are compromised and the extent to which they will survive).

Where a purchaser buys the assets from an insolvent debtor, liabilities remain with the debtor, apart from certain employment liabilities that may transfer to the purchaser in accordance with TUPE (see question 34).

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In liquidations, a distribution will be made when sufficient funds are available to justify it. An administrator can also make distributions to preferential, secured and unsecured creditors (but only with the

sanction of the court in the case of unsecured creditors unless it is a distribution of the prescribed part). Distributions can be made on an interim and a final basis. In the case of a reorganisation, the terms of any distribution will usually be set out in the restructuring agreement, the scheme or in the CVA proposals, as appropriate.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

There are two main types of transaction that may be set aside by a liquidator or administrator under the Insolvency Act. These are transactions at an undervalue (section 238) and preferences (section 239).

A transaction at an undervalue is a transaction entered into for no consideration or for consideration that is significantly less than the consideration provided by the company. A liquidator or administrator can apply to the court for an order restoring the position to that which it would have been in the absence of such a transaction. It is a defence to a claim if the company entered into the transaction in good faith for the purpose of carrying on the business of the company, and there were reasonable grounds for believing that the transaction would benefit the company.

A company grants a preference where it does something, or allows something to be done, that puts a creditor, surety or guarantor in a better position than it would otherwise have been in if the company went into insolvent liquidation. The court will, however, only make an order restoring the position to what it would have been if the company was influenced by a desire to put that other person in that better position. This desire to prefer is assumed where the parties are 'connected' (as defined in the Insolvency Act).

The court will not make any order unless, at the time of entering into the transaction at an undervalue, making the preference or granting the floating charge, the company was unable to pay its debts, or became unable to pay its debts as a consequence of the transaction. Insolvency is, however, presumed in the case of a transaction at an undervalue entered into with a connected person.

In addition to transactions at an undervalue and preferences, certain floating charges will also be invalid under section 245 of the Insolvency Act, except to the extent of any valuable consideration (being money, goods or services supplied; or a discharge or reduction of any debt or interest). No application to court is required.

Separately, an administrator or a liquidator may apply to the court to set aside an extortionate credit transaction. Further, a liquidator, administrator or a 'victim' of the transaction, may challenge any transaction that is entered into at an undervalue where the purpose of making the transaction was to put assets beyond the reach of a person who is making or may make a claim against the company (section 423 of the Insolvency Act).

Under English law, there are no specific legislative provisions that allow for transactions to be annulled as a result of a reorganisation (unless such reorganisation utilises an administration process).

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The 'suspect period' for a transaction at an undervalue or a preference given to a connected party is the two years prior to the 'onset of insolvency'. With respect to a preference given to an unconnected party, the suspect period is six months prior to the onset of insolvency.

The suspect period for the avoidance of floating charges is 12 months prior to the onset of insolvency for a floating charge created in favour of an unconnected party and two years prior to the onset of insolvency for a floating charge created in favour of a connected party.

The provisions setting out what constitutes the onset of insolvency are detailed, but, in summary, relate to the commencement of either administration or liquidation proceedings. Where liquidation is preceded by an administration, the onset of insolvency is the date of commencement of the administration proceedings.

The three types of transactions outlined above can only be challenged in an administration or a liquidation, and not in any other form of restructuring, and the challenge can only be made by the administrator or the liquidator.

The timescale for challenging a transaction defrauding creditors is not limited except for the usual limitation periods unrelated to insolvency. A liquidator, administrator or a 'victim' of the transaction may challenge such a transaction.

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### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The company's officers and directors will not generally be personally liable for obligations of their corporations unless they have entered into personal guarantees. However, the company's officers can be held to be personally liable to contribute to the company's assets for any one of the following reasons:

- misfeasance or breach of any fiduciary or other duty;
- fraudulent trading: section 213 of the Insolvency Act provides that where it appears that any business of the company has been carried on with intent to defraud creditors or for any fraudulent purpose, the court may declare that any persons who were knowingly parties to the carrying on of business in that manner are liable to contribute to the company's assets. This section goes beyond directors and officers and applies to anyone who has been involved in carrying on the business of the company in a fraudulent manner. Actual dishonesty must be proved. Both a liquidator and an administrator can bring this action; and
- wrongful trading: section 214 of the Insolvency Act applies only to directors, former directors and 'shadow directors' and only where such a director continues to trade after a time when he or she knew, or ought to have concluded, that there was no reasonable prospect of the company avoiding insolvent liquidation, or insolvent administration (see also question 13).

The remedies for some of the above claims that may be brought against the directors are designed to be compensatory for the liabilities incurred by the company.

The company's officers can also be criminally liable under sections 206 to 211 of the Insolvency Act for fraud, misconduct, falsification of the company's books, material omissions from statements and false representations. They are also liable to disqualification from being a director of any company for up to 15 years under the Company Directors Disqualification Act 1986. A director can also be disqualified in Great Britain if he or she has been convicted of (amongst others) an offence in connection with the promotion, formation, management, liquidation or striking off of a company outside Great Britain. Lastly, environmental and health and safety legislation may provide for personal liability on directors and officers.

Directors owe a duty to act in the best interests of the creditors (as opposed to the shareholders) in the 'twilight period' (ie, when a company is insolvent or on the brink of insolvency). Previously a common law duty, this duty now also appears in section 172(3) of the Companies Act 2006.

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### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

In principle, each corporate entity has its own existence and the corporate veil will only be rarely pierced so the circumstances where a parent or affiliated company could be liable for its subsidiaries or affiliates are few. There are certain, limited, exceptions to this principle, for example as relates the powers of the UK Pensions Regulator (see question 35) or in relation to certain environmental, health and safety or antitrust matters.

A parent company can be held liable for the acts of a subsidiary pursuant to the law of agency; however, there is no presumption that a subsidiary is the agent of the parent company. In very limited circumstances the English courts will permit the piercing of the corporate veil to allow action to be taken against those who control a company.

A parent company may also be liable for the acts of its subsidiaries under the torts of conspiracy and negligence. In particular, there can be a primary, direct duty of care on a parent company to employees (and potentially others) affected by the activities of a subsidiary under the tort of negligence. A parent could also be held liable if it is considered a person instructing an unfit director – this could be the case where the parent is taken to have exercised the requisite amount of influence over a director who, as a result of acting on the parent's directions or instructions, got disqualified under the Company Directors Disqualification Act 1986.

A parent company could be held liable for fraudulent trading or, if it has acted as a shadow director, for wrongful trading under sections 213 and 214 of the Insolvency Act respectively.

The concept of distributing a group company's assets pro rata without regard to the specific corporate entities infringes the fundamental concept that each company has its own legal entity and that creditors are creditors of the respective company with which they have contracted, and not creditors of a group. This fundamental concept will be lifted in cases of fraud or where there is a deliberate intention to put assets beyond the reach of creditors.

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### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There are no equitable subordination rules as such in English insolvency law, as is the case in certain other European jurisdictions. The rules for distribution of an insolvent estate are set out in the Insolvency Act and Insolvency Rules, and shareholders are last in the order of distribution in respect of their share capital, after unsecured creditors have been satisfied in full. Non-arm's length creditors will rank *pari passu* with the remainder of the unsecured creditors unless they have security, in which case they will rank in accordance with the security ranking.

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### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

A secured creditor can potentially enforce his or her security outside of court proceedings either by the appointment of a receiver or an administrative receiver. A receiver is appointed over specified assets charged by way of a fixed charge. An administrative receiver is appointed where the secured creditor has a charge over the whole or substantially the whole of the company's assets and accordingly has wider powers to run the company, although his or her primary duty will be to the secured creditor. As a result of the Enterprise Act 2002, the use of administrative receivership has been abolished in all but certain limited circumstances for floating charges created after 15 September 2003. The administrative receiver, although an agent of the company, is primarily concerned with the recovery of sufficient assets to pay out to the debenture holder. The almost inevitable consequence of the appointment of an administrative receiver is that the company will go into liquidation as all or nearly all its assets are likely to be realised to repay the secured creditor.

A secured creditor with a qualifying floating charge may also appoint their choice of administrator (which may be done using an out-of-court procedure).

A mortgagee may take physical possession of the property subject to the mortgage, and (where such property is not subject to consumer protection legislation) such possession does not require a court order. Similarly, pursuant to the Financial Collateral Arrangements (No. 2) Regulations 2003, should the security subject to the arrangement become enforceable, the parties may agree that the collateral-taker has the right to appropriate (ie, become the absolute owner of the collateral). However, in certain circumstances relief from forfeiture may be available (and the appropriation may be set aside).

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**Corporate procedures**


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**45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

In addition to a members' voluntary liquidation, a company may be dissolved under sections 1000 and 1003 of the Companies Act 2006, without the need for a formal liquidation procedure if it is dormant and has no assets or liabilities.

Companies that have been dissolved under these sections, as well as companies that have been dissolved following liquidation, may be restored to the Register of Companies on a court application by an interested party within six years of the date of dissolution. A court application may be made at any time for the purpose of bringing proceedings against the company for damages for personal injury.

The court will make an order for restoration if at the time of the dissolution the company was carrying on business or in operation, if (in the case of a voluntary striking off) the company did not comply with the procedural requirements for dissolution or, in other cases, if the court considers it just to do so. A common ground to restore a company is where an asset has become available to the company (eg, a tax refund) that can only be claimed by the company.

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**Conclusion of case**


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**46 How are liquidation and reorganisation cases formally concluded?**

In the case of a voluntary liquidation, once the company's affairs are fully wound up the liquidator must send final accounts showing how the liquidation has been conducted to creditors. After the account has been laid, the liquidator will send a copy of the account to the Registrar of Companies. The company is then deemed to be dissolved at the expiry of three months.

In the case of a compulsory liquidation, if the liquidator is not the official receiver, once the liquidation is complete, the liquidator must present his or her report of the winding up to the creditors. The liquidator must then notify the Registrar of Companies that the final meeting of creditors has been held or that the final account has been sent out. The company is deemed to be dissolved three months after the Registrar of Companies registers this notice. If the liquidator is the official receiver, the liquidation will end three months after the official receiver notifies the Registrar of Companies that the liquidation is complete. Alternatively, if the company has insufficient assets to cover the costs of the liquidation and it appears to the official receiver that the affairs of the company do not require any further investigation, the official receiver may apply to the Registrar of Companies for early dissolution of the company in liquidation.

There are various exit routes from administration. If the objective of the administration is achieved, the administration must be terminated. However, an administration can also be converted into a creditors' voluntary liquidation or the company could be dissolved.

CVAs, schemes and informal reconstructions, if successful, will end in accordance with their terms.

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**International cases**


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**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**
**Recognition and assistance for foreign insolvency proceedings**

There are various tools available to a foreign office holder to obtain recognition of the foreign insolvency proceeding in England, depending on the circumstances of the foreign proceeding: under Council Regulation (EC) No. 1346/2000 on Insolvency Proceedings (the EC Regulation); Regulation (EU) 2015/848 of the European Parliament and of the Council on Insolvency Proceedings (the Recast Regulation) – this regulation is in force at the time of writing although the majority of its provisions will only apply from 26 June 2017; under the Cross-Border

Insolvency Regulations 2006 (the CBIR); under the common law; and under section 426 of the Insolvency Act. Following a withdrawal by the UK from the European Union, these options are likely to be different – however, much will depend on the exit negotiations and any replacement arrangements put in place. English proceedings may be required to establish the foreign office holder's authority to deal with assets in England. Recognition of a foreign insolvency office holder's position will, in itself, confer standing on the office holder to represent the foreign company in the English courts. The office holder may bring proceedings in the English courts in the name of the foreign company and, generally, administer the assets of the foreign company present in England.

The EC Regulation has direct effect in all member states of the European Union with the exception of Denmark. Under the EC Regulation insolvency proceedings are to be opened in the jurisdiction where a debtor has his or her COMI. Such insolvency proceeding will then be automatically recognised as a main proceeding under the EC Regulation in all member states (except for Denmark). In jurisdictions where a debtor has an establishment, secondary or territorial proceedings can be opened which again will be recognised throughout the European Union (save for Denmark). For further detail on the EC Regulation, see the European Union chapter.

The CBIR implemented the UNCITRAL Model Law on Cross-Border Insolvency in Great Britain (ie, excluding Northern Ireland). The CBIR entitle a foreign insolvency representative to apply directly to the British courts to commence British insolvency proceedings, to participate in British insolvency proceedings, and to seek recognition and relief for foreign insolvency proceedings. Foreign proceedings will be recognised as 'foreign main proceedings' where insolvency proceedings have been opened in the jurisdiction where the debtor's COMI is located. Like in the EC Regulation there is a rebuttable presumption that a debtor's COMI is in the place of its incorporation. If insolvency proceedings have been opened in a jurisdiction where the debtor has an establishment only the insolvency proceedings will be designated 'foreign non main proceedings'. Relief is automatic in the case of recognition as a foreign main proceeding and includes an automatic stay and discretionary in the case of a foreign non main proceeding. To the extent there is a conflict between a provision in the EC Regulation and a provision in the CBIR, the relevant provision of the EC Regulation will prevail.

Under the common law, English courts have traditionally promoted the concept of 'modified universalism'. Universalism is the concept that insolvency proceedings in relation to a debtor should apply worldwide, so that there is only ever one main insolvency proceeding in which all creditors are entitled to participate in. 'Modified universalism' qualifies the concept of universalism by giving local courts the discretion to evaluate the fairness of home country procedures and, where necessary, protect the interests of local creditors.

Section 426 of the Insolvency Act allows a 'relevant country or territory' (the Channel Islands, the Isle of Man or any country or territory designated by the Secretary of State – mostly Commonwealth countries but with certain notable exceptions, such as India) to apply to the English courts for assistance. This assistance is wide-ranging and can include the making of an administration order.

**Foreign creditors**

Foreign creditors will be able to provide evidence of their claims in an English liquidation in the normal way. However, if there is a concurrent liquidation of the same company in the foreign jurisdiction, then a creditor proving its claim in England will only be entitled to share in any distribution once any amount received in the foreign proceedings have been taken into account. Foreign currency debts are converted into sterling under mandatory provisions of the Insolvency Act.

**Recognition of judgments (not judgments opening insolvency proceedings)**

Again, there are a number of tools available to obtain recognition of a judgment: the EC Regulation; the common law; and the Brussels Regulation recast (1215/2012). In addition, regard should be had to the Civil Procedure Rules and the different tools available to litigators in England to enforce a foreign judgment (such as the Foreign Judgments (Reciprocal Enforcement) Act 1933).

### Update and trends

The UK has voted to leave the European Union on 23 June 2016. The leave vote does not immediately change the legal backdrop of the restructuring market. No change to the status of EU-derived law in the UK results directly from the leave vote or from the service of the article 50 notification. The UK will remain a member state until it concludes an agreement in relation to its withdrawal from the EU or the two-year article 50 notification period expires (whichever occurs first) (Brexit). Unless replacement legislation is given effect before Brexit, we expect that there will no longer be automatic recognition of UK insolvency proceedings in other EU member states. Reliance will need to be had on each member state's domestic law – as was the case before the EC Regulation on Insolvency Proceedings came into existence in 2002. As regards recognising foreign insolvency proceedings, the UK already has avenues that foreign office holders can use to obtain recognition. While the impact of Brexit on the use of schemes is difficult to predict, we believe these are unlikely to be impacted by Brexit in a material way. This is on the assumption that schemes continue to be enforceable in any relevant EU member states. The details of Brexit consequences for the legal framework of the restructuring and insolvency sphere will be analysed once the specific terms of Brexit are known.

Under the EC Regulation, judgments that concern the course and closure of insolvency proceedings and compositions approved by that court shall be recognised without further formalities. Automatic recognition is also available for judgments that derive directly from the insolvency proceedings and which are closely linked to them (even if they are handed down by another court).

The common law rule that judgments in personam are recognised only where a defendant is present in the foreign jurisdiction when proceedings are initiated, is a claimant or counterclaimant in the proceedings or has submitted to the jurisdiction of the foreign court also applies in an insolvency context (see *Rubin and another v Eurofinance SA and New Cap Reinsurance Corporation (in liquidation) and another v Grant and others* [2012] UKSC 46).

The Brussels Regulation recast (1215/2012) came into effect on 10 January 2015 and is in essence a revised version of Brussels Regulation (EC 44/2001) on the jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. The Brussels Regulation recast applies to litigation commenced on or after 10 January 2015, and judgments given in proceedings commenced on or after 10 January 2015. The old Brussels Regulation continues to apply only to judgments given (pre or post-10 January 2015) in litigation that was commenced pre-10 January 2015. The Brussels Regulation and its recast provide rules for the recognition and enforcement of foreign judgments of contracting states. The Brussels Regulation and its recast do not apply to bankruptcy proceedings relating to the winding up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings.

The FCA Regulations restrict the ability of the court to recognise a foreign insolvency order. Regulation 15A prevents a court from making a recognition or enforcement order under section 426 of the Insolvency Act (or the common law) that would be prohibited by the regulations.

### International insolvency treaties

See above. The UK is party to the EC Regulation and has adopted the UNCITRAL Model Law on Cross-Border Insolvency.

### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

The EC Regulation provides that main insolvency proceedings are to be opened in the member state which that company has its COMI. There is a rebuttable presumption that a company's COMI is where its registered office is located. This is slightly modified in the EC Regulation recast that states that it is not possible to rely on the rebuttable presumption where a debtor has moved its COMI in the preceding three months. In the case of *Interedil (Interedil Srl v Fallimento Interedil Srl and*

*Intese Gestione Crediti SpA (C-396/09)* the European Court of Justice (ECJ) confirmed that COMI must be interpreted in a uniform way by EU member states and by reference to EU law and not national laws. Therefore the English courts will be bound to interpret COMI in a way that is consistent with the interpretation given by the ECJ.

Where a company's registered office and place of central administration are in the same jurisdiction, the registered office presumption set out in the recitals to the EC Regulation cannot be rebutted. Where a company's central administration is not in the same place as its registered office, the presence of assets belonging to the debtor and the existence of contracts for financial exploitation of those assets in an EU member state, other than that in which the registered office is situated, are not sufficient factors to rebut the registered office presumption. This is unless a comprehensive assessment of all the relevant factors makes it possible to establish, in a manner that is ascertainable by third parties, that the company's central administration is located in that other EU member state. Factors that have been held to be relevant to determine a debtor's COMI (in addition to the rebuttable registered office presumption) are: location of internal accounting functions and treasury management, governing law of main contracts and location of business relations with clients, location of lenders and location of restructuring negotiations with creditors, location of human resources functions and employees as well as location of purchasing and contract pricing and strategic business control, location of IT systems, domicile of directors, location of board meetings and general supervision. The relevant date to determine a company's COMI is the date when the request to open the proceedings is made (*Re Staubitz-Scheiber (C-1/04)* and *Interedil* (see above)).

COMI is determined on an entity-by-entity basis.

The Model Law, as applied in the United Kingdom by virtue of the CBIR (see above at question 47) also uses the concept of COMI. The Model Law (like the EC Regulation) does not define COMI but notes that the concept derives from the EC Regulation.

### Cross-border cooperation

#### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Yes, provided certain standing requirements are met – see further in question 47. On occasion, courts have refused to recognise foreign proceedings. For example, *Re Stanford International Bank Ltd (in liquidation)* [2010] EWCA Civ 137, the Court of Appeal refused to recognise a US receiver on the basis of its consideration of where the company had its COMI (using an interpretation of COMI that was consistent with its interpretation under the EC Regulation). Instead, the court recognised the appointment of an Antiguan liquidator as foreign main proceedings. In the case of *Global Distressed Alpha Fund 1 LP v PT Bakrie Investindo* [2011] EWHC 256 (Comm), the High Court held that it had no power to hold that an English law guarantee was discharged by the guarantor's Indonesian debt reorganisation plan. It should be noted that this case is very specific on its facts as the law on the discharge of guarantees is clear.

While not directly relevant to the laws of England and Wales, the Privy Council held (in a case on appeal from Bermuda) in the case of *Singularis Holdings Ltd v PricewaterhouseCoopers (Bermuda)* [2014] UKPC 36 that while there was a common law power to cooperate and assist a foreign liquidator in his or her conduct of insolvency proceedings in a different jurisdiction, such power does not extend to providing a liquidator with a power that he or she did not have in his or her home jurisdiction.

The English courts have in recent years tended to row back from an earlier tendency to grant cooperation and relief based on the common law. As such, there is now a more limited relief available in England than a decade ago – despite this, where relief is possible to be granted under specific legislation the English courts will be willing to do so.

**Cross-border insolvency protocols and joint court hearings**

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

Insolvency protocols have been used in cross-border insolvencies between the United Kingdom and the United States to harmonise proceedings, for example, in 1991 in the *Maxwell Communications Corporation* case.

In the *Lehman Brothers* case, it was clear that due to the volume and size of the claims involved, and the international dimension of the business, international cooperation would be paramount. In 2009, Lehman Brothers administrators in several jurisdictions signed a protocol that focused on cooperation and exchange of information. Crucially, the English administrators did not sign the protocol. In a report to creditors, the English administrators said it was not in the best interests of the English Lehman Brothers entity to 'be party to or bound by such a broad arrangement'. Under the changes to the EC Regulation the use of protocols is specifically sanctioned so it remains to be seen whether such formal legislative blessing of the concept will result in more protocols being implemented.



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# European Union

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The European Union is a unique economic and political partnership among 28 European countries that together cover much of the continent. The EU was created in the aftermath of the Second World War. The first steps were to foster economic cooperation, the idea being that countries that trade with one another become economically interdependent and so more likely to avoid conflict. The result was the European Economic Community (EEC), created in 1958, and initially increasing economic cooperation between six countries: Belgium, Germany, France, Italy, Luxembourg and the Netherlands. Since then, a huge single market has been created and continues to develop. The following countries are currently members of the EU: Austria, Belgium, Bulgaria, Croatia, Cyprus, the Czech Republic, Denmark, Estonia, Finland, France, Germany, Greece, Hungary, Ireland, Italy, Latvia, Lithuania, Luxembourg, Malta, Netherlands, Poland, Portugal, Romania, Slovakia, Slovenia, Spain, Sweden and the United Kingdom (as at the time of writing, the UK remains part of the EU – see ‘Update and trends’).

At the EU level, there are a number of different legislative frameworks in operation in the insolvency context, but by far the most important is the EC Regulation on Insolvency Proceedings (Council Regulation (EC) No. 1346/2000) (the EC Regulation). This came into force on 31 May 2002 and will continue in effect until 26 June 2017 when the majority of the provisions of the Recast to the EC Regulation (the Recast) (which came into force on 25 June 2015) become effective. There is separate legislation for more niche subject matters, such as insurance and credit institutions, which together complement the EC Regulation.

The EC Regulation applies to those insolvency proceedings commenced in the EU (except for Denmark) that are listed in Annex A to the EC Regulation. The EC Regulation does not seek to harmonise the substantive insolvency law of the different EU member states but aims to establish common rules on cross-border insolvency proceedings, based on principles of mutual recognition and cooperation.

It distinguishes between two types of proceedings: main insolvency proceedings (main proceedings) and territorial or secondary proceedings. Main proceedings are opened in the courts of the member state within the territory of which the debtor has its ‘centre of main interests’ (COMI). The EC Regulation does not contain a definition of ‘COMI’ but the recitals to it state that the COMI should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties. In the case of *Interedil Srl v Fallimento Interedil Srl and Intese Gestione Crediti SpA (C-396/09) (Interedil)* the European Court of Justice (ECJ) confirmed that COMI must be interpreted in a uniform way by EU member states and by reference to EU law and not national laws. Where a company’s registered office and place of central administration are in the same jurisdiction, the registered office presumption set out in the recitals to the EC Regulation cannot be rebutted. Where a company’s central administration is not in the same place as its registered office, the presence of assets belonging to the debtor and the existence of contracts for financial exploitation of those assets in an EU member state, other than that in which the registered office is situated, are not sufficient factors to rebut the registered office presumption, unless a comprehensive

assessment of all the relevant factors makes it possible to establish, in a manner that is ascertainable by third parties, that the company’s central administration is located in that other EU member state.

The ECJ has held that the date on which a debtor’s COMI is decided is the date when the request to open the proceedings is made. Main proceedings will encompass all of the debtor’s assets, regardless of where they are situated, and will affect all of the debtor’s creditors.

Secondary and territorial proceedings can be opened in a member state other than the one where the debtor’s COMI is located provided that the debtor has an ‘establishment’ in that jurisdiction. An establishment is defined in the EC Regulation as a place of operations where the debtor carries out a non-transitory economic activity with human means and goods. Secondary proceedings can only be opened once main proceedings have already been opened and are currently (under the EC Regulation) restricted to winding-up proceedings (this restriction is lifted in the Recast). Territorial proceedings can be opened where main proceedings have not yet been opened and are not restricted to winding-up proceedings. The situations in which territorial proceedings can be opened are, however, limited to situations in which there are objective factors preventing main proceedings from being opened or where territorial proceedings in a particular member state are requested by a creditor who is based in such member state or whose claim arises from a debtor’s establishment in that member state. In the event that main proceedings are opened, existing territorial proceedings are converted into secondary proceedings. Both secondary and territorial proceedings are restricted to the assets of the debtor situated in the territory of that member state. The office holders in the main proceedings and the secondary proceedings have a duty to communicate and cooperate with each other.

The EC Regulation is confined to provisions that govern jurisdiction of insolvency proceedings and judgments that are delivered directly on the basis of insolvency proceedings and are closely connected with such proceedings. If an action is not closely connected with insolvency proceedings (even if brought by an insolvency office holder or against an insolvent company), different regimes may apply, such as the Regulation on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (Regulation of the European Parliament and the Council No. 1215/2012 (the Brussels Regulation) – which is a recast of Council Regulation (EC) No. 44/2001) and came into effect on 10 January 2015. The EC Regulation and the Brussels Regulation are designed to complement each other – with insolvency proceedings being specifically excluded from the ambit of the Brussels Regulation. The Brussels Regulation recast applies to litigation commenced on or after 10 January 2015, and judgments given in proceedings commenced on or after 10 January 2015. The old Brussels Regulation continues to apply only to judgments given (before or after 10 January 2015) in litigation that was commenced before 10 January 2015. The Brussels Regulation and its recast provide rules for the recognition and enforcement of foreign judgments of contracting states.

The Recast came into force on 25 June 2015. However, as noted above, the majority of its provisions will not apply until 26 June 2017. Although large sections of the EC Regulation have been rewritten, the cornerstone underpinning the EC Regulation, namely to provide a mechanism for who is to govern the insolvency without harmonising substantive insolvency law across member states, will remain. While

the current text will remain in force until 26 June 2017, the new text will be persuasive should there be any questions of interpretation.

Under the Recast, where a company's registered office has shifted in the three months preceding the filing for proceedings, the rebuttable presumption that COMI is at the same place as the company's registered office will no longer apply. Instead, evidence will need to be provided to demonstrate where a company's COMI is located. Another of the changes is to remove the requirement for secondary proceedings to be winding-up proceedings. The revision also bolsters the duty to cooperate between office holders and the insolvency courts and introduces the concept of a group coordinator whose task it will be to devise a group coordination plan for members of a group that are in insolvency proceedings. The group coordination plan should recommend a comprehensive set of measures appropriate to an integrated approach to the resolution of the group members' insolvencies and in particular is to contain proposals for measures to be taken in order to re-establish the economic performance and financial soundness of the group, settle intra-group disputes and reach agreements between the insolvency practitioners of the insolvent group members. The group coordination plan must, however, not include any recommendations as to consolidation of proceedings or insolvent estates. Other changes introduced by the Recast include a broadening of the types of proceedings that can constitute main proceedings, to include more pre-insolvency rescue processes, and the introduction of the concept of 'synthetic' secondary proceedings whereby local creditors can be protected without the need for secondary proceedings to be commenced.

There is no single criterion to apply to determine if a debtor is solvent in the European Union, as this is a matter for each member state to determine. In general, some member states have a cash flow-only insolvency test while others have a cash flow and balance sheet test.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The rules in this context vary between member states. Under the EC Regulation, main proceedings are to be opened by the courts of the member state in which the debtor has its COMI. Secondary or territorial proceedings are to be opened by the courts where the debtor has an establishment (see question 1). Any restrictions are a matter for individual member states.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The entities that are excluded from customary insolvency proceedings, and the legislation applicable to such entities, differ between member states. However, the EC Regulation does cater for certain specific exclusions under EU-level directives described in further detail below.

#### At the domestic level

It is common in many continental jurisdictions for customary insolvency proceedings not to apply to the insolvency or reorganisation of individuals or entities acting in a personal, non-commercial capacity and specific separate regimes will apply to them. By contrast in other jurisdictions (Germany, for example) any natural or legal person in those jurisdictions is subject to the customary insolvency and reorganisation laws.

#### At the EU level

As mentioned in question 1, the EC Regulation does not apply to the winding up of credit institutions or insurance undertakings, which are instead governed by Council Directive 2001/24/EC on the reorganisation and winding up of credit institutions (the Credit Institutions Directive), which entered into force on 5 May 2001, and Council Directive 2001/17/EC on the reorganisation and winding up of insurance undertakings (the Insurance Undertakings Directive), which entered into force on 20 April 2001. As directives, each member state had to transpose the provisions of the directive into national law.

## The Credit Institutions Directive

The aim of this directive is to facilitate reorganisations of or, if impossible, the winding up of branches of the same credit institution as a single legal entity. This directive makes special provision for the single reorganisation or winding up of a failed credit institution within the EU to be commenced in the credit institution's 'home member state'. Unlike the EC Regulation, there is no scope for any independent or secondary proceedings. The Credit Institutions Directive had to be implemented by member states by 5 May 2004.

## The Insurance Undertakings Directive

Like the Credit Institutions Directive, the aim of this directive is to ensure that there is a single set of reorganisation measures or insolvency proceedings for insurance undertakings with their head office in the EU. Again, the proceedings are to be commenced in the home member state of the insurer. The Insurance Undertakings Directive had to be implemented by member states by 20 April 2003.

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Each member state within the EU has its own provisions for the insolvency of a government-owned enterprise, and there is no harmonised system within the EU. In a number of member states, provided the government-owned enterprise is a private limited company, there is no difference in procedure compared with the insolvency of a privately owned entity. The insolvency of a government-owned enterprise would fall within the scope of the EC Regulation.

In some member states (for example, Italy) public entities are exempted from insolvency, or insolvent companies owned by public agencies are not prevented from carrying on business, or both.

## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

There have been a number of legislative initiatives (in particular after the onset of the financial crisis in 2008) at the EU level to attempt to provide more protection for large financial institutions and provide for a way that these could be rescued or reorganised in an orderly way. Set out below are the main pieces of legislation dealing with this topic. Various sector-based pieces of legislation complement the picture (for example, rules on capital requirement).

## The Financial Conglomerates Directive

The directive on the supplementary supervision of credit institutions, insurance undertakings and investment firms in a financial conglomerate (Council Directive 2002/87/EC) (the Financial Conglomerates Directive), came into force on 11 February 2003 and introduced a prudential regime for financial conglomerates moving away from a purely sector-based approach to regulation and looking at systemically important institutions holistically. The directive provides for enhanced cooperation processes (including information sharing) between cross-sector and cross-border supervisors of financial conglomerates, including the appointment of a single lead regulator to act as coordinator and exercise supplementary supervision of each financial conglomerate. In addition, the directive sets out supplementary capital adequacy requirements for certain entities within a financial conglomerate as well as supplemental supervision of risk concentrations.

The Financial Conglomerates Directive has been amended, in particular by Council Directive 2011/89/EU, which entered into force on 9 December 2011. Member states had to implement the majority of the provisions into national law by 10 June 2013.

On 22 December 2014 the Joint Committee of the European Supervisory Authorities published new guidelines on the convergence of supervisory practices relating to the consistency of supervisory coordination arrangements for financial conglomerates. The guidelines aim to clarify and enhance cooperation between the competent authorities on a cross-border and cross-sectoral basis, to supplement the functioning of sectoral colleges where a cross-border group has been identified as a financial conglomerate, and to enhance the level playing field in

the financial market and reduce administrative burdens for firms and supervisory authorities.

In June 2016, the EU Commission launched a consultation on the performance of the Financial Conglomerates Directive within the framework of the regulatory fitness and performance programme. The consultation will inform the EU Commission's evaluation of the Financial Conglomerates Directive, to assess whether the current regulatory framework is proportionate and fit for purpose, and delivering as expected considering its objective of identifying and managing risks that are inherent to financial conglomerates to ensure financial stability. At the time of writing, the consultation was expected to close on 20 September 2016.

### The Single Supervisory Mechanism and the Single Resolution Mechanism

In response to the recent Eurozone debt crisis, the EU institutions agreed to establish a Single Supervisory Mechanism and a Single Resolution Mechanism for banks, based on the European Commission roadmap for the creation of an EU banking union (Banking Union). Banking Union applies to member states that are part of the Eurozone, but non-Eurozone member states can also join. As part of the initiative, Regulation (EU) 806/2014 (the SRM), which establishes uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms and Regulation (EU) 1024/2013 (the Single Supervisory Mechanism Regulation) on the policy of prudential supervision on credit institutions, were adopted.

The SRM creates a centralised resolution system for dealing with failing banks and on 31 December 2015 implemented the EU-wide Bank Recovery and Resolution Directive (see below for further detail) in the Eurozone. The regulation has direct effect and prevails over national law. The SRM confers special authority and powers to a new EU-level authority, the Single Resolution Board (the SRB). The SRB will assess whether an individual bank is failing, or is likely to fail, and prepare for that bank's resolution by devising a resolution scheme, which will provide a framework for the use of resolution tools and the Single Resolution Fund (the SRF), which can be used, among other things, to fund the resolution of failing banks, or the compensation of shareholders and creditors.

### The Bank Recovery and Resolution Directive

In June 2016, the EU Commission introduced a framework for the recovery and resolution of credit institutions and significant investment firms that are considered to be 'too big to fail': the Bank Recovery and Resolution Directive (Directive 2015/59/EU of the European Parliament and of the Council of 15 May 2014 (the BRRD)). The majority of the provisions of the BRRD entered into force on 2 July 2014. The deadline for member states to adopt and publish implementing legislation and regulations was 31 December 2014.

The BRRD is aimed at providing national authorities with common powers and instruments to pre-empt bank and significant investment firm crises and to resolve any financial institution in an orderly manner in the event of failure, while preserving essential bank operations and minimising taxpayers' exposure to losses. The BRRD establishes a range of instruments to tackle potential bank or significant investment firm crises at three stages: preparatory and preventative, early intervention, and resolution.

At the preparatory stage, the BRRD requires firms to prepare (and to annually update) recovery plans (also often referred to as 'living wills') and competent authorities to prepare resolution plans based on information provided by firms. The BRRD also reinforces authorities' supervisory powers.

At the early intervention stage, the BRRD is intended to give powers to supervising authorities to take early action to address upcoming problems. Such powers include requiring a firm to implement its recovery plan (living will) and replacing existing management with a special manager.

At the resolution stage, the BRRD gives supervising authorities powers to ensure the continuity of essential services and to manage a firm's failure in an orderly way. These tools include a sale of (part of a) business, the establishment of a bridge institution (a temporary transfer of good assets to a publicly controlled entity), an asset separation (the transfer of impaired assets to an asset management vehicle) and a bail-in measure (the imposition of losses, with an order of seniority,

on shareholders and unsecured creditors). The sale-of-business tool entails the sale of all or part of the failing entity to a private party. The bridge-institution tool involves selling good assets or essential functions of the entity and separating them into a new bridge entity. The asset-separation tool entails the bad assets of the firm being put into a 'bad bank' (this tool may only be used in conjunction with another resolution tool to prevent the failing entity benefiting from an unfair competitive advantage). The bail-in tool is effectively a process of internal recapitalisation, whereby, for instance, certain eligible liabilities of the failing entity are cancelled, written down or converted into equity, or the principal or outstanding amount of eligible liabilities is cancelled or reduced (this does not apply to certain excluded liabilities such as financial collateral arrangements and liabilities to employees). The aim of the bail-in tool is to shift the costs of a failing entity from the taxpayer to the creditors and shareholders. The BRRD also requires member states to set up a resolution fund to ensure that the resolution tools can be applied effectively.

The BRRD provides several safeguards to protect the position of shareholders and creditors of a failed entity in the event that the resolution authority decides to use resolution tools. One of these is the 'no creditor worse off' principle. This principle means that the writedown or conversion of capital instruments of a failing entity, or the application of another resolution tool on a failing entity, may not result in its shareholders or creditors being worse off than they would have been had the entity been wound up under normal insolvency proceedings. Compliance with this 'no creditor worse off' principle is assessed after the completion of the resolution phase. The resolution authority must appoint an independent third party that will assess whether shareholders and creditors are worse off. If that is the case, then such shareholders and creditors have the right to be compensated for their losses (the compensation will be paid from the SRF).

In October 2015 the EU Commission issued a press release stating that it had decided to refer six member states (the Czech Republic, Luxembourg, the Netherlands, Poland, Romania and Sweden) to the ECJ over their failure to implement the BRRD into national law.

### Recovery and resolution for non-banks

On 5 October 2012, the European Commission published a consultation paper on a possible recovery and resolution framework for financial institutions other than banks. The institutions concerned are financial market infrastructures (central counterparties and central securities depositories, insurance and reinsurance firms and payment systems (such as TARGET2 and CHAPS)) and other non-bank entities such as payment institutions and electronic money institutions. The consultation closed in December 2012. In October 2013 the European Parliament passed a resolution on recovery and resolution plans for non-bank institutions. Among other things, the European Parliament urged the European Commission to prioritise recovery and resolution of central counterparties and of those central securities depositories that are exposed to credit risk.

On 9 February 2016, then EU Commissioner Jonathan Hill gave a speech on priorities for an approach to resolution for central counterparties, stating that the EU would align work in this area with the work being taken forward as part of the G20 agenda. On 7 March 2016, the EU Commission published a list of planned initiatives for 2016, which envisaged that legislation on the recovery and resolution of central counterparties would be adopted in the fourth quarter of 2016.

### Banking sector structural reform

On 29 January 2014 the Commission adopted a legislative proposal for a regulation on the structural reform of the banking sector. The regulation is to introduce measures improving the resilience of EU credit institutions. Banks falling within the scope of the proposed regulation will be prohibited from conducting proprietary trading and may be required to separate the performance of certain risky activities from the performance of banking activities deemed to be more socially useful, such as deposit-taking. On 19 June 2015, the Council of the EU agreed its stance for negotiations with the European Parliament in relation to the proposal, stating that the proposed regulation would apply only to banks that are either deemed of global systemic importance or exceed certain thresholds in terms of trading activity or absolute size. The proposal has been debated both in the European Parliament's Committee on Economic and Monetary Affairs (ECON Committee) and the Council

and has been heavily criticised. Negotiations between the Commission, the Council and the European Parliament will begin as soon as the European Parliament has determined its position.

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### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

Each member state within the EU has its own provisions for the creation of security, both in type and procedure required (including any steps to perfect such security). There is no harmonised system for the creation of security within the EU. However, generally, in each EU member state it is possible to take a mortgage or fixed charge over immoveable (real) property and such security is capable of, and will usually cover fixtures and fittings relating to the immoveable (real) property. There is usually a registration requirement for the security to be effective.

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### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

As noted in question 6, each member state has its own provisions for the creation of security and there is no harmonised system for the taking of security within the EU. However, common types of security include:

- liens;
- possessory pledges;
- non-possessory pledges (in some jurisdictions, the concept of the pledge has been refined so that the security can exist but physical delivery, a characteristic normally associated with a pledge, is not required in order for the security to be effective);
- chattel mortgages – similar in nature to the possessory pledge;
- security assignments – an assignment of personal property to the secured party;
- fixed charges – providing security over a particular asset or class of assets;
- floating charges (or equivalent) – security over all of the assets and undertakings of the chargor; and
- reservation of title.

Other types of security include:

- rights of privilege granted by law;
- special liens only given to secure medium or long-term bank facilities;
- assignments of receivables; and
- cash collateral charges.

#### Effect of insolvency proceedings on security rights

The EC Regulation specifically addresses third parties' rights in rem and states (article 5(1)) that the opening of insolvency proceedings in one EU member state will not affect the rights in rem of creditors or third parties in respect of tangible or intangible, moveable or immoveable assets belonging to the debtor that are located in a member state other than the one in which the proceedings are commenced.

#### The Financial Collateral Arrangements Directive

Council Directive 2002/47/EC on financial collateral arrangements (the Financial Collateral Arrangements Directive) came into force on 27 June 2002. The purpose of the Financial Collateral Arrangements Directive was to simplify the process of taking financial collateral across the EU by introducing a minimum uniform legal framework. As a directive, each member state had to transpose the provisions into national law by 27 December 2003. Financial collateral under the directive is made up of cash, financial instruments and credit claims. The directive provides for rapid and non-formalistic enforcement procedures designed in part to limit contagion effects in the event of default by one of the parties to the arrangement. Member states may not make the creation, perfection, validity, enforceability or admissibility of a financial collateral arrangement dependent on the performance of any formal act. In addition, member states have to ensure that the collateral taker is able to realise financial collateral in one of the following manners: if it concerns financial instruments, by sale or appropriation and by setting off their value against, or applying their value in discharge of, the relevant financial obligations; if it concerns cash, by setting off the amount against or applying it in discharge of the relevant financial obligations;

and if it concerns a credit claim, by sale or appropriation and by setting off their value against, or applying their value in discharge of, the relevant financial obligations. Appropriation is possible only if this has been agreed in the arrangement. The directive also stipulates that certain insolvency provisions do not apply. Financial collateral arrangements may not be declared invalid or void or be reversed on the sole basis that they have been concluded or that the financial collateral has been provided on the day of the commencement of winding-up proceedings or reorganisation measures, but prior to the order or decree making that commencement; or in a prescribed period prior to, and defined by reference to, the commencement of such proceedings or measures or by reference to the making of any order or decree.

In the case of *Private Equity Insurance Group v AS Swedbank C-156/15*, following a request for a preliminary ruling from the Supreme Court of Latvia, Advocate General Szpunar gave an opinion on whether financial collateral is limited to collateral provided in securities payment and settlement systems; the proper interpretation of the requirement for control; and whether the collateral taker can realise financial collateral notwithstanding the commencement or continuation of winding up proceedings, thereby essentially overriding *pari passu* distribution to creditors.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

The treatment of unsecured creditors in an insolvency process varies between member states. In general, unsecured creditors in the EU have limited remedies against debtors because of their unsecured status. To have any recourse to a debtor's assets, prior to the commencement of formal insolvency proceedings, a creditor would generally have to bring its own proceedings in a local court and obtain a judgment debt against the debtor, which, if not complied with, may give scope for recourse against the debtor's assets themselves. The treatment of unsecured creditors in the context of pre-judgment attachments varies between member states. In many jurisdictions, it is open to creditors to obtain a pre-judgment attachment or freezing order over some or all of a debtor's assets in order to prevent the relevant assets being dissipated pending a trial or resolution of a claim or claims. As a precaution, however, such an order is usually made subject to the provision of some kind of security or bond to protect the debtor in the event that it is later established that the attachment or freezing order was granted incorrectly.

In many jurisdictions, however, it is open to certain creditors in possession of relevant rights to assert a possessory lien or other similar claim, which would circumvent the requirement to bring legal proceedings. It is also possible in some jurisdictions for creditors to avail themselves of the benefit of retention of title provisions.

On 17 May 2014, Regulation (EU) 655/2014 established the European Account Preservation Order (EAPO). The EAPO can be used by a creditor to freeze some or all of the funds within any bank account held by a debtor located in another member state within the EU than that of the creditor. An EAPO operates to stop the withdrawal or transfer of the funds of a bank account beyond the amount specified in the order. EAPOs are to be used in cross border claims as an alternative to other methods of preservation available in the individual member states. Regulation (EU) 655/2014 will apply from 18 January 2017 to those member states which have not opted out (the United Kingdom has opted out of the regime).

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

The procedure for, and effects of, a voluntary liquidation vary between member states. For a solvent company, the usual position for member states in the EU is that the members can put the company into liquidation by resolving to do so through a general meeting. For an insolvent company, the usual position is that the directors must apply to the court to commence the liquidation process and the debtor is required to show that it is unable to pay its debts as they fall due or that its liabilities exceed its assets or both.

While the rules vary between member states, in certain member states (for example, France) commencing a voluntary liquidation case will cause a moratorium to arise, preventing creditors from starting or continuing any proceedings against the debtor while it is in a process and in some jurisdictions, the debtor will be put under the control of a liquidator or other insolvency office holder. In some jurisdictions any secured creditors will have an unrestricted right to exercise their security during this process but in others such rights are restricted or subject to certain conditions, depending on the type of security in question and the particular type of proceeding the debtor is in.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

The requirements for, and effects of, the involuntary liquidation process vary between member states. Generally, in order for a creditor to make a successful petition for the involuntary liquidation of a debtor, the creditor is required to demonstrate that the debtor is unable to pay its debts as they fall due or that the debtor's liabilities exceed its assets.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Voluntary reorganisations can be classified as 'insolvency proceedings' under the EC Regulation, provided that the particular type of reorganisation is specified in the annexes to the EC Regulation (for example, the *saueguard* procedure in France is included in Annex A to the EC Regulation and therefore falls within its ambit). While the relevant requirements vary between member states, the general requirement is for the debtor to show that it is likely to become insolvent in the near future if steps are not taken to restructure its business and generally the debtor will also be required to show that there is a real expectation that the business can be rescued or that the attempt to reorganise the company and its affairs will ultimately result in a better outcome for its creditors.

An English law scheme of arrangement is a major exception to this by allowing for a 'cram down' of minority creditors if it is not possible to obtain unanimous creditor consent to proposals for reorganisation. Notwithstanding this, the scheme of arrangement has not been designated as an insolvency process for the purposes of the EC Regulation (including the Recast).

When the new text comes into force in June 2017 (see question 1) the scope of the EC Regulation will be expanded to include collective proceedings, including interim proceedings, which are based on a law relating to insolvency and in which, for the purpose of rescue, adjustment of debt, reorganisation or liquidation, the debtor is totally or partially divested of its assets and an insolvency office holder is appointed or the debtor's assets and affairs are subject to the control or supervision by a court or a temporary stay of individual enforcement proceedings is granted by a court or by operation of law in order to allow for negotiations between the debtor and its creditors, provided that these proceedings provide for suitable measures to protect the general body of creditors and are preliminary to one of the proceedings that fall within the scope of the EC Regulation if no agreement is reached. The scope will thus be expanded and allow more interim and rescue proceedings to be designated to fall within the scope of the EC Regulation. Each member state has designated which procedures fall within the scope of the Recast.

Voluntary reorganisations do not necessarily have to be implemented through any formal restructuring procedure and therefore there is significant variation in terms of the prerequisites to implementation. Voluntary reorganisation can be implemented as a result of informal negotiations with creditors outside of the usual formal restructuring procedure; such informal arrangements will be governed by the laws of the relevant jurisdiction or the laws and terms of agreements being compromised. In some jurisdictions, however, the formal requirements may be relatively strict.

The effect of a debtor's voluntary reorganisation on the debtor itself and its creditors varies between member states. Some potential scenarios include the management remaining free to run the business or an administrator or other insolvency office holder being appointed.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

While the position varies between member states, the general position is that a creditor cannot instigate an involuntary reorganisation (as opposed to an involuntary liquidation; see question 10) of the debtor. In Germany, however, a creditors' meeting may instruct the insolvency office holder to produce a reorganisation plan.

The effects of the commencement of an involuntary reorganisation vary between member states.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

The position as to whether an obligation to file for insolvency exists, at which point it arises and the potential liabilities that can be incurred if such obligation is not met varies significantly between member states. There is no statutory requirement in England and Wales to commence insolvency proceedings for example (although the potential for director liability for wrongful trading effectively imposes such an obligation in given circumstances, albeit not an express one), whereas in Germany there are stringent mandatory insolvency filing rules for directors including clear time limits.

The position on liabilities varies between member states. Where there is a failure to meet an obligation to file for insolvency, the potential consequences can include personal liability for losses caused by such failure, a fine or imprisonment for directors of the company or both. The consequences of carrying on business while insolvent vary according to each member state. In some jurisdictions, civil liability may attach to the directors, for example, in England for wrongful trading. In other member states a failure to file for insolvency when the relevant insolvency test is met may result in criminal liability.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

The rules vary among member states. Where a reorganisation is implemented under the supervision of the court a debtor will be able to carry on its business subject to court-imposed conditions. Depending on the jurisdiction and the particular process, an insolvency office holder could be appointed (either by the court or out of court) to run the debtor's business and there will be rules specific to the relevant jurisdiction and process governing the way in which the office holder may run the business and his or her powers and duties.

The rules regarding the conditions that apply to the use or sale of the assets of the business vary between member states and depend on the type of insolvency procedure the debtor is undergoing.

In various jurisdictions creditors who supply goods or services after the commencement of a formal reorganisation procedure will have priority over other creditors (France, for example) but this will often depend on the specific arrangements made with those particular creditors and the relevant local law.

The roles of the creditors and the court in supervising the debtor's business vary between member states and depend on the particular insolvency process that the debtor is in. The creditors do not generally have a formal supervisory role in the proceedings but will often have voting power depending on the relevant insolvency process and the relative size of a creditor's stake. In many jurisdictions an insolvency office holder appointed by the court will supervise the debtor's business activities on the court's behalf.

The powers that directors and officers can exercise after insolvency proceedings have been commenced vary according to both the type of insolvency process and member state. For example, in an English administration process, a director may no longer exercise a management power without the consent of the administrator. In a French safeguard proceeding on the other hand the directors retain management and control of the company.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

The rules on stays of proceedings and moratoria vary between member states. Under the EC Regulation, the effect of insolvency proceedings on the continuation of proceedings by individual creditors is expressly a matter for the law of the member state where those proceedings are opened. The exception to this is that the effect of insolvency proceedings on a pending action relating to an asset or right where the debtor has been divested of that asset or right will be governed by the law of the member state where the relevant action is pending. Under the Recast, arbitration proceedings are specifically included within this exception, which codifies the existing position in a number of member states.

The ability may vary between local courts, and a court could impose a stay on transfers by the debtor of its property, a freeze on creditor enforcement action and judicial proceedings against the debtor or a stay on other creditor rights.

The circumstances and process in which creditors may obtain relief from such prohibitions varies between member states.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Post-filing credit procedures vary significantly between jurisdictions and the EC Regulation does not specifically address this issue.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

The rules on set-off and netting in this context vary between member states, and the EC Regulation states that the conditions under which set-offs may be invoked shall be determined by the laws of the member state in which proceedings are opened.

Notwithstanding the variation in the rules on set-off across the EU, the EC Regulation does contain a specific provision relating to set-off, which seeks to preserve each member state's laws on set-off, primarily by stating that 'the opening of insolvency proceedings shall not affect the right of creditors to demand the set-off of the claims against the claims of the debtor, where such a set-off is permitted by the law applicable to the insolvent debtor's claim'. Contractual netting is not specifically addressed under the EC Regulation.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

The procedure for the sale of assets during reorganisations or liquidations varies between member states. However, the EC Regulation provides that a disposal of an immovable asset, a ship or an aircraft subject to registration in a public register, or any registered securities, in each case after the opening of insolvency proceedings, will be governed

by the law of the member state where the particular asset or register is located.

The relevant documentation effecting the reorganisation will provide for the terms under which the assets or the whole of the business are disposed of.

The question of whether or not assets are purchased 'free and clear' or subject to encumbrances will depend on the relevant local legislative framework. The Council 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 (the Acquired Rights Directive) aims to safeguard and protect the rights of employees on a 'change of employer' and provides that in certain situations where there is a transfer of a business, the rights and obligations under a contract of employment will also transfer automatically. As a directive, each member state had to transpose the provisions contained in the Acquired Rights Directive into national law. On 10 April 2015, the European Commission launched a public consultation at EU level, with representatives of employers and employees, on the possible consolidation of three EU directives on worker information and consultation, one of which was the Acquired Rights Directive. However, most responses to the consultation opposed a revision or recasting of the directives, arguing that the existing directives work well for both employers and workers. At the time of writing, it is understood that the proposed consolidation will not be going ahead.

The position on the permissibility of credit bidding in insolvency sale processes varies between member states.

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

Where the IP right is a right that has been registered (or is pending registration) at EU level, rather than on a national level (eg, a 'Community trademark' or 'Community patent'), the EC Regulation provides that such a right may only be included in the debtor's main insolvency proceedings (not in secondary or territorial proceedings, even where no main proceedings have commenced). The law of the member state where main proceedings are opened will therefore determine the insolvency office holder's rights in relation to that IP right. Other IP rights can be included in secondary or territorial proceedings.

The rules in some jurisdictions (Italy, France and Germany, for example) prohibit the automatic termination of contracts upon an insolvency (which would include agreements containing IP rights) and render void any clauses purporting to achieve this effect. In other jurisdictions (England, for example) it is possible to provide for an agreement to terminate automatically on insolvency, but its validity and effectiveness will greatly depend on the drafting of the clause.

The rules regarding whether an insolvency office holder can continue to use IP rights granted under an agreement with the debtor vary between member states.

The power of an insolvency office holder to terminate an IP agreement varies between member states.

The Recast specifies that for the purposes of the EC Regulation, a European patent with unitary effect, a Community trademark or any other similar right established by Union law may be included only in main proceedings. The Recast also states that European patents are treated as being situated in the member state for which they are granted, and copyright and related rights are treated as being situated in the member state where the owner has its habitual residence or registered office.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The EU rules on data protection have their origins in Directive 95/46/EC of the European Parliament and of the Council of

24 October 1995 on the protection of individuals with regard to the processing of personal data and on the free movement of such data (the Data Protection Directive), which has been transposed into national law by individual member states. As a directive, each member state had to transpose the provisions into national law by 24 October 1998.

A data controller is required to comply with the data protection principles set out in the Data Protection Directive, as transposed into national law, when processing any personal data. The first such data protection principle is that personal data must be processed fairly and lawfully. Where valuable customer data are collected by the insolvent company, it is one of the assets that an insolvency office holder is able to realise for the benefit of creditors. Member state data protection laws will apply and an office holder may require a buyer of the data to comply with all the seller's obligations under those laws and to provide an indemnity to the seller and the office holder against any liability for failure to have complied. This may be supported by an agreed form 'fair processing' notice, which the buyer will be required to send to each customer to inform the customer that the buyer is now the data controller and of any new purposes for which the customer's personal data will be processed by the buyer.

As the Data Protection Directive sets out minimum standards to be transposed into national law, the Data Protection Directive has not been implemented consistently and there may be additional requirements under different member state laws. A new EU Regulation on data protection will apply directly in all member states from May 2018, at which point it will repeal the Data Protection Directive; however, national data protection laws on areas not covered by the Regulation may continue to apply.

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#### Rejection and disclaimer of contracts in reorganisations

**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

The rules governing the disclaimer and rejection of unfavourable contracts vary between member states. In certain jurisdictions an insolvency office holder is permitted to disclaim onerous contracts without the need for a court order (for example, England) while in other jurisdictions it may be possible to apply to the insolvency court to terminate any contract where the debtor has outstanding obligations if the court is of the view that this constitutes a convenient outcome for the insolvency proceedings (for example, in Spain). Special arrangements are usually in place in employment contracts and these will vary between jurisdictions.

The rules regarding contracts that may not be rejected and the procedure to reject a contract vary between member states.

The effects of breach of contract post-insolvency vary between each member state and often there is a distinction to be drawn between contracts entered into by the insolvency office holder (where a breach may result in damages with high priority ranking) or contracts entered into by the company prior to insolvency (where a breach may only result in an unsecured claim against the company).

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#### Arbitration processes in insolvency cases

**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

The Recast specifically states that the effects of insolvency proceedings on pending arbitral proceedings concerning an asset or a right that forms part of a debtor's insolvency estate are to be governed solely by the law of the member state in which the arbitral tribunal has its seat.

The rules governing the effect of insolvency proceedings on individual creditor proceedings vary between member states. Generally, the use of arbitration proceedings in EU member state insolvency proceedings is relatively limited. Once insolvency proceedings are commenced, the moratorium that normally arises will generally restrict

other actions and the use of other legal processes, including arbitration therefore making arbitration sometimes not available as a process.

The rules governing whether arbitration proceedings can be continued differ. In England, for example, once a company enters into administration, the administrator or the court must give permission for other legal proceedings to be commenced or continued against the company. In contrast, in Germany the commencement of insolvency proceedings does not lead to automatic cessation of arbitration proceedings (although the insolvency administrator will be the right party rather than the insolvent company).

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#### Successful reorganisations

**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

The mandatory features of a voluntary reorganisation have been covered in greater detail in question 11.

Generally, the different classifications of preferential, secured and unsecured creditors is used. The number and value of those creditors that will be required to instigate a reorganisation can range from a bare majority to 75 per cent.

In some jurisdictions it is possible for non-debtor parties to be released from liability but the rules are different in each EU member state.

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#### Expedited reorganisations

**24 Do procedures exist for expedited reorganisations?**

The procedural elements will be dictated by the law of the jurisdiction where proceedings are commenced. Practically speaking, a large proportion of reorganisations are implemented as a result of informal negotiations with key creditors outside of a formal restructuring framework and therefore the parties to the discussions and the particular circumstances of the debtor and creditor base dynamic will dictate the timetable. In some jurisdictions a reorganisation can be planned and implemented very quickly (for example, England) although no separate procedure is required for the expedited process. In other jurisdictions, a formal procedure for an expedited reorganisation exists (for example, France).

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#### Unsuccessful reorganisations

**25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

This is more a practical than a legal question. In general, any proposed reorganisation will fail if the requisite support of each of the various different creditor or stakeholder classes is not obtained. In some jurisdictions the court may be willing to grant an interim stay on creditor actions to allow a reorganisation to be implemented.

The rules will vary between jurisdictions but the effects on the debtor if the reorganisation plan is not approved can be wide-ranging, including an agreement from key creditors to a temporary relaxation of the debtor's obligations, or the debtor entering into liquidation or another form of insolvency process.

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#### Insolvency processes

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

The procedural requirements of the various types of insolvency proceedings that exist in different member states (including, eg, in respect of notices to be provided to creditors, what meetings should be held, the ambit of information provided to creditors or any creditors' committee, etc) vary between member states.

The EC Regulation contains specific provisions relating to the provision of information to creditors and the lodgement of creditors'

claims in relation to insolvency proceedings covered under the EC Regulation. The Recast also provides for a standard claim form to be introduced across the EU. This will be available to any 'foreign creditor' (being a creditor having its habitual residence, domicile or registered office in a member state other than the member state of the opening of proceedings) wishing to lodge a claim (although this is not compulsory).

Once insolvency proceedings have been commenced, the office holder or the court must inform all known creditors in all member states, including in such notice necessary information on the procedure for making claims, the relevant time limits for making such claims and any penalties for late filing of claims. Creditors are notified by either personal notice or advertisement and a creditors' meeting is normally held early on in the process.

In the majority of member states, a further meeting with creditors will be held to consider and approve the claims of creditors as well as a final meeting in which the final accounts of the debtor are approved and the liquidation ends. In some cases a reorganisation plan will be presented during the liquidation and a separate creditors' meeting may be convened in order to discuss the plan and vote on it.

Creditors do not normally have standing to pursue any remedy of the debtor against third parties, however, in some jurisdictions it is open to creditors (normally through the creditors' representative and depending on the type of insolvency process the debtor is in), to bring direct proceedings against former directors or shadow directors of the debtor in their personal capacity for losses they have incurred as a result of the director's or shadow director's conduct, as opposed to the insolvency office holder making such a claim on behalf of the debtor.

Whether a reorganisation plan can provide for the release of liabilities owed by third parties who are not part of the debtor group will vary between insolvency processes and member states.

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### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

The rules on whether creditors may pursue the remedies of a debtor's estate vary between member states. In Spain, for example, where an insolvency office holder decides not to exercise a particular remedy open to him or her that is in the interests of the estate, the creditors may file an application to seek such a remedy. While the rules relating to third-party funding of litigation are different in each member state, often an alternative route is for the creditors to group together to provide funding for the costs of the insolvency office holder or the estate (as applicable) incurred in exercising the remedy, making the relevant claim or taking the relevant action.

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### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The rules governing creditor representation vary between member states. In a number of member states (England, Germany, Italy and Austria, for example) there will often be a creditors' committee that assists and supervises the insolvency office holder in the exercise of his or her duties. The creditors' committee will be appointed by the competent court or by the creditors as a group directly, where permitted. If a creditors' committee is formed the committee is free to retain its own advisers but there is no EU-wide rule as to how the costs of such advisers are funded.

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### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Under the EC Regulation, it is possible to open main proceedings in relation to each individual company. There is a limited duty of cooperation of office holders in the main and secondary proceedings but there

is no express duty of insolvency office holders of main proceedings to cooperate where the companies are part of a corporate group. Generally speaking, the assessment of where a debtor's COMI is located is applied on an entity-by-entity basis, and therefore different rules apply to different entities in respect of their insolvency proceedings, but the rules in some member states (Spain, for example) allow group companies to make joint filings for insolvency in certain circumstances.

The English decision *In the matter of Nortel Networks* (2009) (where the group operated through companies incorporated in a number of EU jurisdictions but the filing was made in England on the basis of an English COMI), recognised that the best course of action may sometimes be a coordinated approach to group insolvency. Practically speaking, group insolvencies are generally managed in this way but this approach will only work if the companies have a common COMI, allowing for the appointment of a common insolvency office holder.

As regards a creditor of a number of group entities, the English courts confirmed in *Re Alitalia Linee Aeree Italiane SpA* (2011) that a creditor of a company can lodge a claim in both that company's main and secondary proceedings. The priority of that creditor's ranking in any distribution will however differ depending on the jurisdiction of the relevant proceedings. There are some instances where the courts of one jurisdiction will consider applying the order of priority of another jurisdiction (for example, in the English case of *MG Rover*), but this is generally exceptional and will not happen unless there is a significant benefit to the administration and realisation of value. In *Comité d'entreprise de Nortel Networks and others* (2011), the ECJ ruled that, where a company is in both main and secondary proceedings, the courts of member states in which main and secondary proceedings have been opened both have concurrent jurisdiction to determine which of the company's assets fall within the secondary proceedings. Where both courts purport to exercise this jurisdiction, the first decision in time will be binding.

The rules in the context on whether assets can be transferred from an insolvency administration in one country to an administration in another vary between member states.

The fact that the EC Regulation does not currently provide for group insolvencies has been recognised and addressed in the Recast. This introduces a separate chapter dealing with the insolvency of members of a corporate group. The chapter deals with two aspects: first, it increases the cooperation that is to take place between members of a company that are in insolvency procedures. Second, it establishes the concept of a group coordination plan for members of a group of companies.

As regards cooperation, the Recast enhances cooperation between insolvency office holders as well as courts supervising respective insolvencies. An insolvency office holder appointed over one member of a corporate group is to cooperate with an insolvency office holder appointed to another member of the same group to the extent that such cooperation is appropriate to facilitate the effective administration of the proceedings, is not incompatible with the rules applicable to such proceedings, and does not entail any conflict of interest. The use of agreements or protocols between insolvency office holders is officially envisaged and blessed. The intended aim of the cooperation is that information which may be relevant to the other proceeding is immediately communicated and that possibilities of restructuring the group are explored and, where such possibilities exist, these are coordinated with respect to the proposal and negotiation of a coordinated restructuring plan. In addition, an office holder appointed in insolvency proceedings for one member of a corporate group is given rights aimed at encouraging a group-wide rescue.

As regards the group coordination plan, any insolvency office holder appointed over a group member of companies can request the court having jurisdiction of the insolvency of that group member to open group coordination proceedings. (Where multiple courts are asked to open group coordination proceedings the court first seised is to have jurisdiction.) The request is to be accompanied by: a proposal on who is to be nominated the group coordinator; an outline of the proposed group coordination plan; a list of the insolvency practitioners appointed in relation to group members and, where relevant, the courts involved in the insolvency proceedings of the group members; and an outline of the estimated costs of the proposed group coordination and an estimation of the share to be paid by each group member. A court seised with a request to open group coordination proceedings shall open these if it is satisfied that: the opening of such proceedings is

appropriate to facilitate the effective administration of the insolvency proceedings relating to the different group members; no creditor of the group member anticipated to participate is likely to be financially disadvantaged by such participation; and the proposed coordinator is eligible under the law of a member state to act as an insolvency practitioner. The proposed group coordinator may not be one of the insolvency office holders appointed in respect of other group members and must not have a conflict of interest in respect of the group members, their creditors and the insolvency office holders appointed over group members. When opening group coordination proceedings the court must appoint a coordinator, decide on the outline of the coordination and decide on the estimation of costs and the share to be paid by each group member.

The group coordinator so appointed is to: identify and outline recommendations for the coordinated conduct of the insolvency proceedings; and propose a group coordination plan that recommends a comprehensive set of measures appropriate to an integrated approach to the resolution of the group members' insolvencies. In particular, the plan may contain proposals for: measures to be taken in order to re-establish the economic performance and financial soundness of the group; the settlement of intra-group disputes as regards intra-group transactions and avoidance actions; and agreements between the different insolvency office holders. However, the coordination plan must not include recommendations as to any substantive consolidation of proceedings or estates. The remuneration of the coordinator is to be 'adequate, proportional to the tasks fulfilled and reflect reasonable expenses'. The coordinator must also establish the final statement of costs and the share to be paid by each group member.

An insolvency office holder of any group member may object to the inclusion in the group coordination proceedings of the proceedings in respect of which it has been appointed, or to the person to be appointed as group coordinator. National law is to dictate the approval requirements (if any) that an insolvency office holder will need to obtain to decide whether or not to participate in the group coordination plan. Where an office holder decides not to participate, the group coordination proceedings will not have any effect on that group member. Where an office holder has agreed to be part of the group coordination proceedings, he or she will need to consider the coordinator's recommendations but is not obliged to follow them or the group coordination plan (but would need to give reasons why he or she is not following the plan).

## Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

The rules governing rights of appeal vary between member states, and are a matter for the law of the member state where the insolvency proceedings are opened. In England, for example, court orders made in insolvency proceedings follow the ordinary course for appeals.

## Claims

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

In certain jurisdictions the creditor's claim is submitted to the court (for example, Austria, where creditors file their claims with the court, and these are then accepted or rejected by the insolvency office holder), whereas in others (England, for example) claims are submitted directly to the insolvency office holder for review and processing.

The rules in the majority of jurisdictions provide for reasonably stringent time limits applicable to the submission of claims. Failure to submit a claim within the prescribed time limits may, in some jurisdictions, result in the debt owed to the relevant creditor or creditors being extinguished and any security rights lost.

In those jurisdictions where claims are submitted to the court, the court will generally hold a hearing to review the claims and rule on them. In those jurisdictions where claims are submitted to the

insolvency office holder directly, the office holder will review, assess and process the claims and notify the creditors of the result.

The majority of jurisdictions allow for an appeal against the rejection of a claim, however, the requirements differ from jurisdiction to jurisdiction.

Under the EC Regulation, each creditor, wherever domiciled in the EU, has the right to assert claims against the debtor's assets in each relevant insolvency proceeding.

Typically, EU jurisdictions allow for a transfer of insolvency claims. The requirements vary between member states as to the necessity to disclose the transfer of the claim.

The rules regarding whether claims for contingent or unliquidated amounts can be recognised and how the amounts of such claims are determined vary between member states. Similarly, whether a claim acquired at a discount can be enforced for its full value will depend on the rules in member states. The question of interest accrued post-insolvency varies between member states and the EC Regulation does not address this point. In England, for example, post-insolvency interest is subordinated until provable debts have been paid.

Under the Recast, a single EU-wide standardised claim form is to be introduced. Any foreign creditor (being a creditor having its habitual residence, domicile or registered office in a member state other than the member state of the opening of proceedings) may lodge its claim using this standard claim form, which will indicate, among other things, the creditor's name and address, the nature and amount of the claim, details of any interest being claimed, whether any preferential status is claimed, whether security in rem or a reservation of title is alleged in respect of a claim and whether any set-off is claimed and the amount net of the set-off. If a creditor lodges its claim by means other than the standardised claim form, the claim must contain the information that would be contained in the standard claim form. Claims will be able to be lodged in any of the official languages of the EU although the creditor may be required to provide a translation into any official languages of the state of the opening of the proceedings or into another language that the member state has accepted. Each member state must indicate whether it accepts any official EU language other than its own for the purposes of accepting claims. Claims are to be lodged in the period stipulated by the law of the member state of the opening of the proceedings, but in the case of a foreign creditor, that period must be at least 30 days from the publication of the opening of proceedings in the insolvency register of the state of opening of the proceedings.

In addition, under the Recast, where the court, insolvency office holder or debtor in possession has doubts in relation to a claim, he or she is to give the creditor the opportunity to provide additional evidence on the existence and the amount of the claim.

## Modifying creditors' rights

**32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

The claims that are to be lodged against a debtor's estate and the ranking of claims vary between member states and are matters for the law of the state where the insolvency proceedings are commenced.

The ability of the courts to vary the priority of creditor claims varies between member states. In England, for example, the power available is limited to changing the order of a specific list of insolvency expenses. There may be challenges to the security of a purported secured creditor that, if successful, could result in a secured creditor's claim being deemed to be unsecured. However, this is not strictly a reordering of a predefined order of distribution but a reclassification of where a particular creditor sits in that ranking, based on an assessment of the relevant facts.

## Priority claims

**33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

The majority of jurisdictions afford some measure of priority for certain tax and other governmental claims. The majority of jurisdictions also provide that the costs of the insolvency process and the insolvency office holder's fees and expenses are paid out first. Whether these

claims have priority over all secured creditors, or only some, varies between member states.

Under the EC Regulation each creditor, wherever domiciled in the EU, has the right to assert claims with regard to the debtor's assets in each pending insolvency proceeding (ie, in main and secondary proceedings). This right extends to each member state's taxation and social security authorities but does not give these claims automatic priority status. A taxation authority enjoying priority status as a preferential creditor under its domestic laws is likely to be able to prove only as an ordinary unsecured creditor in proceedings in other member states.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

The provisions for dealing with employees' salaries during a restructuring or liquidation vary between member states. Generally, most countries have some form of protection in place for ensuring that there are funds available to pay (part of) outstanding salaries. Directive 2008/94/EC of the European Parliament and of the Council of 22 October 2008 on the protection of employees in the event of the insolvency of their employer (the Employment Insolvency Directive) protects employees who have a claim for unpaid remuneration against an employer who is in a state of insolvency. The directive requires member states to establish guarantee institutions that guarantee payment of employees' claims and, where appropriate, severance pay on termination of employment relationships. Member states are permitted to set ceilings on (and time limits for) the payments made by the relevant guarantee institution.

Some jurisdictions protect employees' rights arising after insolvency proceedings have commenced, whereas others require provision only to be made for claims arising before proceedings were opened.

In some jurisdictions there is a requirement for a certain amount of money to be ring-fenced for employees or that an employee's claim is to be ranked as preferential.

In addition, the Acquired Rights Directive provides that in certain situations where there is a transfer of a business, the rights and obligations under a contract of employment will also transfer automatically (see question 18). This can mean that the employee claims (even for back pay) transfer to the (presumably solvent) transferee/purchaser and so are reflected in a lower price paid for the relevant business (and so with less assets available for other creditors). However, where the transfer takes place during insolvency proceedings that have been opened in relation to a transferor but not 'with a view to the liquidation of the assets of the transferor', and provided that such proceedings are under the supervision of a competent public authority (which may be an insolvency office holder determined by national law), member states may provide that the transferor's debts arising from any contracts of employment or employment relationships and payable before the transfer or before the opening of the insolvency proceedings shall not be transferred to the transferee, provided that such proceedings give rise to protection for employees equivalent to that set out in the Employment Insolvency Directive. This is the approach taken in England and Wales, for example.

If the insolvency proceedings have been opened 'with a view to the liquidation of the assets of the transferor', the Acquired Rights Directive allows member states to exclude employee liabilities from transferring altogether.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

The provisions for dealing with pension-related claims against employers in insolvency proceedings vary among member states. Member states have very different approaches to pensions, regardless of whether they are internal to the company or guaranteed by a third-party insurer (for example, in Germany). In the latter case the insolvency of the employer company should not therefore affect the protection of the pension fund. Some jurisdictions include pension liabilities as preferential claims, in others in the absence of any special circumstances, pension-related claims rank as an unsecured debt. Other jurisdictions

deal with pensions by way of a statutory guaranteed fund (for example, Germany). There is no EU-wide regulation on how a pension deficit (whether it is an actuarial deficit or unpaid pension contributions) is to be treated in the ranking of insolvency claims.

The Employment Insolvency Directive requires member states to ensure that necessary measures are taken to protect the interests of employees and previous employees in respect of rights conferring on them immediate or prospective entitlement to benefits under supplementary occupational or inter-occupational pension schemes outside the national statutory social security schemes. The interpretation of this requirement has been considered by the ECJ in the cases of *Robins v Secretary of State for Work and Pensions* (C-278/05) and *Hogan v The Minister for Social and Family Affairs, Ireland and the Attorney General* (C-398/11). These cases confirm that the Employment Insolvency Directive does not necessarily require accrued pension rights to be funded by member states themselves or to be funded in full, but does seem to require that employees and former employees must receive no less than 50 per cent of their accrued old-age benefits where both the employer and pension scheme are insolvent. The amount of any state pension to which an employee or former employee is entitled cannot be taken into account when calculating what proportion of their accrued old-age benefits they should receive under the Employment Insolvency Directive. The Court of Appeal in England and Wales recently made a reference to the ECJ on whether the limits under the UK statutory Pension Protection Fund (PPF) comply with the requirements of article 8, given that the PPF includes a cap on compensation that can result in some cases in it being much less than 49 per cent (*Hampshire v PPF* [2016] EWCA Civ 786).

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Much of individual member state law in respect of environmental liabilities is derived from EU legislation. The EU has a designated environmental policy set out in articles 191 to 193 of the Treaty on the Functioning of the European Union. EU policy is based on the precautionary principle and on the principles that preventive action should be taken, that environmental damage should as a priority be rectified at source and that the polluter should pay.

Most EU environmental legislation centres on the concept of placing liability on the 'operator' of a particular plant. EC Directive 2008/1/EC concerning integrated pollution prevention and control provides for the imposition of obligations for compliance with its substantive provisions on the 'operator' being any natural or legal person who operates or controls the installation or whether this is provided for in national legislation to whom decisive economic power over the technical functioning of the installation has been delegated. Directive 2000/76/EC on the incineration of waste, Directive 1999/13/EC on the limitation of emissions of volatile organic compounds because of the use of organic solvents in certain activities and installations, and, with slight modifications, Directive 96/82/EC on the control of major accident hazards involving dangerous substances and Directive 1999/31/EC on the landfill of waste all use the concept of placing liability on the operator. Under Directive 2004/35/EC on environmental liability with regard to the prevention and remedying of environmental damage, provision is made for non criminal liability for clean-up costs. This directive also requires member states to take measures to encourage the use by operators of appropriate insurance or other forms of financial security and the development of financial security instruments and markets in order to provide effective cover for financial obligations under the directive to cover their potential insolvency.

As these legislative measures are set out in directives they required each member state of the European Union to implement the legislation into domestic legislation.

The EC Regulation does not deal with the impact of environmental liabilities on insolvency and therefore each member state must enact appropriate legislation in this regard (drawing on the above directives and their national implementation). The rules between member states vary and often also vary depending on the type of insolvency process

or the identity of the person who caused the environmental liability (eg, whether it was caused by the company pre-insolvency or by the company while in an insolvency process), or both, and whether, for example, an office holder can disclaim a contract where environmental liability attaches.

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### Liabilities that survive insolvency proceedings

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#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

The rules in respect of the survival of liabilities in an insolvency or reorganisation vary between member states. Where the debtor is reorganised pursuant to some form of insolvency plan (for example, a scheme of arrangement under English law or an insolvency plan under German law), the debts of the debtor will usually survive only to the extent specified in the scheme of arrangement or insolvency plan. Certain insolvency procedures do not, however, bind certain types of creditors (typically secured or preferential) unless they vote in favour of the procedure. The treatment of employment liabilities upon the transfer of the debtor's business and assets is the subject of the Acquired Rights Directive (see question 18).

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### Distributions

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#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

The rules governing the distribution of proceeds from the realisation of assets will be dictated by the insolvency laws in the relevant member states.

In liquidations, once claims have been admitted or rejected and preferential and secured claims have been dealt with, provided there are sufficient assets left to pay unsecured creditors, the remaining funds will be distributed *pari passu* to all unsecured creditors.

In most jurisdictions, reorganisations are treated differently. Distributions will then be made in accordance with the terms of the plan agreed with creditors.

Under the EC Regulation and in order to ensure equal treatment of creditors, the distribution of assets is coordinated by the office holder of the main proceedings under the 'hotchpot' rule. This rule requires that where a creditor, after the opening of the main insolvency proceedings by any means (including enforcement) obtains total or partial satisfaction of its claim out of the assets of the debtor situated in another member state, it must return what it has obtained to the liquidator. This is strengthened by the rule that a creditor who has obtained a dividend on its claim will share in distributions made in other proceedings only where creditors of the same ranking have in those proceedings received a dividend in the same proportion of their claims. This procedure ensures dividends are paid evenly to creditors regardless of the number of jurisdictions in which they have lodged claims. The EC Regulation also attempts to protect the interests of all creditors by empowering the liquidator in the main proceedings to lodge the claims of all creditors in any secondary proceedings where it serves the creditors' interests. Any surplus of assets in the secondary proceedings, after payment of all claims provable under local law, must be remitted to the insolvency office holder in the main proceedings.

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### Transactions that may be annulled

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#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The rules relating to the validity or unenforceability of legal acts detrimental to creditors vary between member states and are a matter for the law of the state where the insolvency proceedings are opened.

Typically, transactions at an undervalue can be set aside, although the relevant period during which a transaction will be vulnerable to challenge prior to the insolvency process varies widely between member states. It is also very common that transactions preferring one creditor over another are vulnerable to challenge, particularly when debts have been paid that have not yet fallen due. Most jurisdictions also make specific provisions for the avoidance of transactions motivated by fraud.

The usual result of a transaction being annulled is that the property in question is required to be returned to the company or its insolvency

office holder. In some jurisdictions, however, the court has very wide discretion as to the orders that can be made, which may go beyond simply requiring return of the property.

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### Proceedings to annul transactions

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#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The rules relating to the voidability or unenforceability of legal acts detrimental to the creditors vary between member states and are a matter for the law of the state where the insolvency proceedings are opened.

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### Directors and officers

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#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The laws governing liability of directors will generally be those of the jurisdiction of incorporation in circumstances where insolvency proceedings are commenced in that jurisdiction. In a scenario where a company's COMI is different from its place of incorporation, the directors will need to be aware of potential liabilities in both jurisdictions. In the recent case of *Kornhaas v Dithmar* [2015] EUECJ C-594/14, the ECJ ruled that the provisions of German company law that (broadly) require directors to file for insolvency within 21 days of a company becoming unable to pay its debts fall within the scope of article 4 of the EC Regulation on Insolvency Proceedings. This meant that the directors of an English incorporated company with its COMI in Germany and that had been placed into insolvency proceedings in Germany could be liable under these provisions to make payments under German law.

Generally, it is possible for directors and officers to be liable to contribute to the debtor's assets but because of the concept of limited liabilities, this is normally limited to where the director's conduct falls below the requisite standard.

Directors can sometimes be made personally liable for pre-insolvency actions. The types of claim for which a director can be liable range from failing to place the company into insolvency at the appropriate time, to fraud. The most common claim, however, is of negligence. There is some variation of the rules between member states as to who can bring claims against directors. In most jurisdictions it is the debtor itself, but in other jurisdictions creditors can bring claims directly against directors for losses they have suffered. Another common claim is that the directors wrongly allowed the debtor to continue to trade despite the fact that the debtor was in a precarious position.

Directors are also exposed to a range of criminal sanctions arising from their conduct prior to insolvency. In some jurisdictions, directors can also subsequently be disqualified from acting as directors for a given time or indefinitely.

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### Groups of companies

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#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Each member state has its own legislation regulating if (and how) a parent or affiliated corporation can be responsible for the liabilities of subsidiaries or affiliates. In general, the starting point is that each corporate entity is self-standing and, because of the principle of limited liability, not responsible for the actions or insolvency of any other group company. This can, however, change in certain circumstances; for example, in England, an affiliated company may be held liable to contribute to a company's pension deficit where certain conditions are met.

Whether a court can order a distribution of group company assets pro rata without regard to the assets of the individual corporate entities involved varies between member states. In some member states, in highly exceptional circumstances a court may order this. For example, in the English case of *Re Bank of Credit and Commerce International SA (No. 3)* the court approved liquidators entering into a pooling agreement stating that it was 'satisfied that the affairs of BCCI SA and BCCI Overseas are so hopelessly intertwined that a pooling of their assets,

### Update and trends

On 23 June 2016, the UK voted to leave the European Union. The vote to leave does not immediately change the legal backdrop to the UK's relationship with the EU. The UK will notify its intention to leave the EU by following the process set out in article 50 of the EU Treaties. Following service of the article 50 notification, the UK will remain a member state until it concludes an agreement in relation to its withdrawal from the EU or the two-year article 50 negotiation period expires (whichever occurs first) (Brexit). On Brexit, the EU will consist of 27, rather than 28, member states – the UK having left. EU legislation as it applies to the EU member states will be unaffected by Brexit (unless as part of the Brexit negotiations, legislation is amended to cater for Brexit). The relationship between the UK and the EU following Brexit will depend on the negotiations between the UK and the EU member states.

The EU Commission has launched an insolvency initiative, aimed at setting common standards across restructuring and insolvency law in member states, and providing tools that would allow viable businesses in distress to be rescued and honest but bankrupt individuals to be given a second chance. On 2 March 2016, the Commission published an inception impact assessment on the initiative. The Commission ran a public consultation on this for 12 weeks, which closed on 14 June 2016, seeking stakeholders' views on key insolvency aspects in the EU to ensure that national insolvency frameworks work well, in particular in a cross-border context. This is a follow-up to the Commission Recommendation of 2014 on a new approach on business failure and insolvency, and is in line with the 2015 Capital Markets Union action plan. The Commission intends to present a legislative proposal on insolvency by the end of 2016.

with a distribution enabling the like dividend to be paid to both companies' creditors, is the only sensible way to proceed. It would make no sense to spend vast sums of money and much time in trying to disentangle and unravel'. In other member states (Austria, for example) regardless of whether group companies are considered to be one economic entity, the principle of legal separation is to be respected in all circumstances and the transfer of assets between several insolvent debtors (even within the same group) is prohibited.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

The principle of equitable subordination exists in a number of member states (for example, Austria whereby certain debts (for example, repayment of loans made when the company is in 'crisis') owed to a shareholder are subordinated in a company's insolvency). Different member states, however, have different rules governing the extent of such subordination. In Germany, for example, shareholder loans and shareholder claims resulting from comparable transactions are subordinated in a company's insolvency irrespective of whether they qualify as equity substitution; in addition, repayments made and collateral granted in relation to such shareholder loans within the relevant look-back period are subject to clawback rights.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

The rules in this context vary between member states. In some jurisdictions it is possible for assets to be seized outside of court proceedings. In England, for example, in some situations a secured creditor can appoint an administrative receiver who, while an agent of the debtor, has as his or her primary duty an obligation to recover sufficient assets to repay the debenture holder.

Creditors can also avail themselves of certain 'self-help' remedies against the assets of the debtor themselves, for example, by way of the exercise of a lien, a retention of title clause or the appropriation of assets (potentially by way of a pledge). These remedies are considered in further detail in questions 7 and 8.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

In general, there are procedures for the liquidation or dissolution of a corporation outside of the insolvency process, particularly where the company's constitutional documents or by-laws (as applicable) provide for this. Some possible scenarios include the company expiring at the end of a fixed duration or being wound up after achieving the purpose for which it was established or where it can no longer achieve the purpose for which it was established.

There are some provisions of European law in specific contexts that would be relevant (cross-border mergers, for example), but these are not of general application.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

In nearly all jurisdictions, liquidation proceedings will end with a court hearing or meeting at which the final accounts of the company will be approved.

Reorganisation cases usually come to an end either when the dividends agreed to under the plan have been distributed or if the debtor goes into liquidation having been unable to comply with the terms of the plan.

On request from the liquidator in the main proceedings, a court in another member state must stay secondary proceedings unless the request is of manifestly no interest to creditors in the main proceedings. Where secondary proceedings can be closed by means of a rescue plan, the liquidator in the main proceedings may propose the plan under the law of the state where those proceedings are opened, otherwise the closure by rescue plan shall not become final without the consent of the liquidator.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

##### Recognition and relief

The EC Regulation governs cross-border insolvency proceedings for member states of the EU (see question 1). Under the EC Regulation, insolvency proceedings opened in a member state where a debtor has its COMI will be automatically recognised as main proceedings in all member states (except for Denmark). In jurisdictions where a debtor has an establishment, secondary or territorial proceedings can be opened, which again will be recognised throughout the European Union (save for Denmark). The judgment opening main proceedings produces the same effects in any member state as under the law of the state of the opening of proceedings (unless secondary proceedings are opened in accordance with the terms of the EC Regulation in a different member state). The recognition or relief currently available in EU countries concerning insolvency proceedings opened in a country outside the EU will depend on the individual approach taken by each country.

##### Treatment of foreign creditors

The EC Regulation specifies that any creditor who has his or her habitual residence, domicile or registered office in a member state other than the state of the opening of proceedings (including the tax authorities and social security authorities of member state) have the right to lodge

claims in the insolvency proceedings. The treatment of foreign creditors outside the scope of the EC Regulation depends on the laws in each member state.

### Recognition of foreign judgments

Under the EC Regulation, judgments that concern the course and closure of insolvency proceedings and compositions approved by that court shall be recognised without further formalities. Automatic recognition is also available for judgments that derive directly from the insolvency proceedings and that are closely linked to them (even if they are handed down by another court). The EC Regulation however only deals with insolvency matters (see question 1). Recognition of a foreign non insolvency related judgment may be available under the Brussels Regulation (see question 1) which provides rules for the recognition and enforcement of foreign judgments of contracting states.

The Brussels Regulation and its recast do not apply to bankruptcy proceedings relating to the winding up of insolvent companies or other legal persons, judicial arrangements, compositions and analogous proceedings. In recent cases before the English courts, parties have argued (relying on foreign expert opinions) that an English law-governed scheme of arrangement should be recognised in other European Union member states because of the provisions of the Brussels Regulation. (A scheme of arrangement is not listed in the Annex to the EC Regulation and does not fall within the scope of the EC Regulation, hence does not benefit from automatic recognition in other member states.) Courts in other member states may need to consider the recognition in particular of schemes of arrangement and the scope of the Brussels Regulation in the future.

Additionally, member states may have special rules for the recognition of foreign judgments and in particular whether registration of these may be required.

### International treaties

Although various EU member states are considering adoption of the Model Law, it has only been implemented by Greece, Poland, Romania, Slovenia and the United Kingdom.

The provisions of the EC Regulation are similar in many respects to the Model Law so within the EU, cross-border recognition operates along similar lines.

### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

The EC Regulation does not contain a definition of 'COMI' but the recitals to it state that the COMI should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties. The EC Regulation

applies the concept of COMI to each individual debtor and not to a group of companies, which can all have individual COMIs.

In the case of *Interedil*, the ECJ confirmed that COMI must be interpreted in a uniform way by member states and by reference to EU law and not national laws. Where a company's registered office and place of central administration are in the same jurisdiction, the presumption that COMI is at the debtor's registered office cannot be rebutted. Where a company's central administration is not in the same place as its registered office, the presence of assets belonging to the debtor and the existence of contracts for financial exploitation of those assets in a member state, other than that in which the registered office is situated, are not sufficient factors to rebut the registered office presumption, unless a comprehensive assessment of all the relevant factors makes it possible to establish, in a manner that is ascertainable by third parties, that the company's central administration is located in that other member state.

To address concerns over 'bankruptcy tourism', the Recast contains provisions whereby if a debtor's registered office has shifted in the three months preceding the filing for insolvency proceedings, the existing rebuttable presumption will no longer apply. In such cases, the debtor will need to produce evidence about COMI to show where it is located. Factors that have been held to be relevant to determine a debtor's COMI (in addition to the registered office presumption) are: location of internal accounting functions and treasury management, governing law of main contracts and location of business relations with clients, location of lenders and location of restructuring negotiations with creditors, location of human resources functions and employees, domicile of directors, location of board meetings and general supervision. The relevant date to determine a company's COMI is the date when the request to open the proceedings is made (*Re Staubitz-Scheiber* (C-1/04) and *Interedil* (see above)).

COMI is determined on an entity-by-entity basis although within the boundaries of member states it is open to member states to make legislation permitting a group of companies to file for insolvency with the same court.

### Cross-border cooperation

#### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

The EC Regulation requires that the office holders in main proceedings and secondary proceedings have a duty to communicate certain information to each other and to cooperate in general (see question 29), for example the secondary proceedings office holder must give the main proceedings office holder an opportunity to submit to it a proposal on how the assets in the secondary proceedings should be used. In practical terms such cooperation is made difficult by the lack of a central



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database across the EU where insolvency proceedings and related court orders are logged. The Recast provides for a national and an interlinked EU-wide database of insolvency proceedings, which will go some way to alleviate this shortcoming.

Outside the court system, office holders in different jurisdictions can also agree to bilateral or multiparty protocols. This type of cooperation has been seen in the multi-jurisdictional administration of Lehman Brothers, where the administrators across a number of jurisdictions attempted to put in place bilateral arrangements for the provision of information or services. The negotiation process was time-consuming and fraught with difficulty.

The Recast addresses these points and provides for enhanced cooperation and formalises the use of protocols (see question 29).

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#### **Cross-border insolvency protocols and joint court hearings**

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

As mentioned in question 1, the EC Regulation was designed to assist with cross-border cooperation between the member states of the EU.

An example can be found in the case of *In the matter of Nortel Networks* (2009) before the English courts, referred to in question 29. The English court found in this case that it had jurisdiction to send letters of request to courts in other member states, requiring notification of an application to open secondary proceedings. The court held that the duty in the EC Regulation on liquidators to cooperate with each other should extend to a wider obligation to cooperate between courts exercising control of insolvency proceedings.

The Recast addresses this point and formalises the use of protocols (see question 29).

# France

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The provisions relating to French insolvency proceedings are codified under articles L610-1 to L680-7 of the French Commercial Code and have been recently reformed by Law No. 2015-990 of 6 August 2015 (the Macron Law) which came into force on 8 August 2015 (some provisions, however, will only become effective at a later date).

Aspects relating to cross-border insolvencies are governed by the EU Regulations No. 1346/2000 and 2015/848 on insolvency proceedings (the EU Insolvency Regulations).

The French insolvency test is a pure cash-flow test, defined as the debtor's inability to pay its debts as they fall due with its immediately available assets, taking into account available credit lines and moratoria.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The courts having jurisdiction over insolvency proceedings will differ depending on whether the debtor conducts a civil or commercial activity. In theory, for commercial debtors (such as limited companies, close corporations, partnerships, limited liability companies or individuals conducting trade activities), the court of first instance is the commercial court located where the debtor has its registered office.

Pursuant to the Macron Law, starting from 1 March 2016 specialised commercial courts have jurisdiction over insolvency proceedings opened against companies which meet the following criteria:

- number of employees exceeding 250 and a turnover exceeding €20 million either at the level of the company against which the insolvency proceedings have been opened or at the level of the group of companies which is controlled by the company against which the insolvency proceedings have been opened; or
- turnover exceeding €40 million either at the level of the company against which the insolvency proceedings have been opened or at the level of the group of companies controlled by the company against which the insolvency proceedings have been opened.

These specialised commercial courts will also have jurisdiction over insolvency proceedings opened in France by foreign companies pursuant to the EU Insolvency Regulations rules.

Pursuant to the EU Insolvency Regulations, foreign entities with no registered offices in France may file a petition for the start of main insolvency proceedings in the court that has jurisdiction where their centre of main interests (COMI) is located.

When the COMI of the debtor is located in another member state (other than Denmark), secondary proceedings can be commenced in France if the debtor has an establishment in France.

For civil debtors (companies of a civil nature and farmers), the relevant court of first instance will be the civil court. The same principles apply to the location of this court as for the commercial court above.

During insolvency proceedings, an insolvency judge is appointed by the court. Such insolvency judge is given certain jurisdictional powers and is in charge of many procedural matters relating to the

proceedings (such as the acknowledgment or rejection of most debt claims filed in the insolvency proceedings).

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Insolvency proceedings set out in the French Commercial Code apply to:

- self-employed individuals;
- corporate entities, whether of a commercial or civil nature;
- merchants; and
- farmers and craftsmen (individuals registered with the *Répertoire des Métiers*, the specific registry for craftsmen).

The only persons excluded from these proceedings are individuals who are not self-employed (employees or civil servants), entities regulated by public law, which are not subject to any specific insolvency proceedings because of their particular status, entities which are not registered with the commercial register and do not have a legal personality (such as *sociétés en participation*, *sociétés de fait*, *sociétés en formation*) and the new type of company entitled *société de libre partenariat* created by the Macron Law.

Article L611-3 et seq relating to mandat ad hoc and conciliation proceedings are available to corporate entities, merchants and craftsmen, but not to farmers or self-employed individuals, who are subject to specific preventive measures.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The procedures followed in the insolvency of a government-owned enterprise will differ depending on whether such enterprise is governed by public law or by private law. Although with respect to some enterprises there is an uncertainty as to whether they are governed by public or private law, it is generally established that: (i) government-owned entities taking the form of industrial and commercial bodies (EPICs) are governed by public law and (ii) companies controlled by public entities (such as state or local authorities), taking the form of a state company, a nationalised company, a semi-public company or a local public company, are governed by private law.

EPICs are not subject to the insolvency proceedings applicable to private law companies and the French legislator has not created any equivalent insolvency proceedings for this type of enterprise. Furthermore, pursuant to article L2311-1 of the General Code on Ownership of Public Entities, EPICs' assets and funds cannot be attached or seized. Nevertheless, instead of implementing the usual methods of enforcement, creditors of EPICs may rely on the specific payment procedure against public entities provided in article 1-II of Law No. 80-539 of 16 July 1980. The objective of this procedure is to enforce a judicial decision ordering a public entity to make a payment for the benefit of one of its creditors.

Publicly owned companies governed by private law may be either wholly owned by public entities (such as a state company, a nationalised company or a local public company) or partly owned by public entities (such as a semi-public company). These types of company are subject to the same insolvency proceedings as the other private commercial companies (although in very limited situations, the assets of some of these companies cannot be seized if they have a public service purpose).

### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

On 26 July 2013, France enacted specific legislation aimed at dealing with the financial difficulties of certain credit institutions and investment firms. This legislation has been recently modified by Ordinance No. 2015-1024 dated 20 August 2015, in order to adapt French law to the European Bank Recovery and Resolution Directive. Pursuant to this legislation, credit institutions and investment firms having a balance sheet that exceeds a certain threshold must prepare – and update each year – a recovery plan to be implemented in the event of financial difficulties (without the support of the French state) and notify such plan to the French banking regulator, the *Autorité de contrôle et de régulation* (ACPR), which in turn is required to prepare a resolution plan for such institutions. If the recovery plan is deemed insufficient, the ACPR may request the institution to modify it and, later, to implement further measures, notably reducing the risk exposure, recapitalising quickly, changing the business or financial strategy, or modifying the legal structure. The ACPR is also given broad powers in order to deal with the financial difficulties of defaulting institutions, including 'bail-in' measures consisting of cancelling or writing off shareholders' equity and cancelling, writing off or converting subordinated debt into equity. Other measures that can be implemented by the ACPR include appointment of a temporary administrator; dismissal of executive officers; transfer of all or part of the assets or business of the defaulting institution; restriction or prohibition on the distribution of dividends; issue of new shares; restriction or prohibition on the carrying out of certain transactions; and payments by the deposit guarantee fund, such fund being financed by contributions by the financial and banking sector. This legislation aims to strengthen the framework for the management of financial crises and at prioritising a restructuring of institutions facing financial problems prior to any grant of public aid.

### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

The most usual type of security taken over immoveable property in France is a mortgage or a lender's lien.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The most common type of security taken over moveable property is a pledge (known as *gage* in respect of tangible assets and *nantissement* in respect of intangible assets). Other types of security are: express contractual provisions relating to retention of title (in the case of asset sales), assignment of receivables by way of security (known as *Dailly* assignments), delegation of receivables, cash collateral and, more recently, security trusts.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Prior to the start of safeguard or insolvency proceedings, provided the debt is overdue, an unsecured creditor may try to obtain an attachment order and to seize one or more of the debtor's assets. In general, unless the seizure is completed prior to the start of safeguard or insolvency proceedings against the debtor, such seizure is stayed during the insolvency or safeguard proceedings. An attachment order can be obtained on an expedited basis.

In the course of safeguard or insolvency proceedings, secured and unsecured creditors will generally be subject to the same rules with respect to the prohibition of payments and the stay of proceedings in relation to pre-insolvency claims (see questions 14 and 15).

No special procedures apply to foreign creditors in this respect.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

An insolvent debtor is required to file a request for the start of insolvency proceedings with the relevant court within 45 days of the date on which it became insolvent (see question 1), unless, on the debtor's request, a conciliator is appointed in the same time period. In order to file for liquidation proceedings, the debtor must show that it is insolvent and that recovery is obviously impossible.

If the court orders the immediate liquidation of the debtor's assets, it will appoint a liquidator and proceed with the sale of the debtor's assets on a piecemeal basis by way of private sale or auction.

Alternatively, where there are prospects that all or part of the assets can be sold as a going concern to a third party, the insolvency court may authorise a temporary continuation of operations for up to six months. In large cases, a judicial administrator will be appointed by the court in addition to the liquidator. Such judicial administrator will be in charge of managing the debtor company and proceeding with the sale of the business during the temporary continuation of the debtor's operations.

The commencement of voluntary liquidation proceedings imposes a stay of payments on the debtor and a stay of proceedings on creditors. In addition, the commencement of the liquidation renders all debts of the insolvent company immediately due (unless a sale of the debtor's business is contemplated during the liquidation proceedings, in which case, the debts will become due upon the expiry of the temporary continuation of the debtor's operations).

Generally, the creditors must file a statement of their claims within two months of the date the court judgment ordering the liquidation of the debtor's assets was published in the Official Gazette for Civil and Commercial Announcements. The time allocated to creditors to declare their claims is extended to four months for creditors residing outside mainland France.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Any unpaid creditor may file an application for the start of liquidation proceedings against a debtor. The creditor must show that it has already tried to obtain payment of its overdue debt (for example, by attempting to seize the debtor's assets) and that the debtor is unable to meet its debts as they fall due. The creditor must also prove that the debtor's recovery is obviously impossible. Liquidation proceedings can also be started at the initiative of the public prosecutor.

The effects of involuntary liquidations are similar to those of voluntary liquidations.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

##### Out-of-court workout proceedings

When a debtor company finds itself in financial difficulties but is not yet insolvent according to the French insolvency test (see question 1), it can ask the court to appoint an insolvency practitioner (in the capacity of *mandataire ad hoc*) to help the management negotiate an amicable restructuring with all or part of its creditors, suppliers and possible new sponsors in the framework of a *mandat ad hoc*. The scope of the *mandataire ad hoc*'s mission is fixed on a case-by-case basis by the court and there is no statutory limitation to the length of the mission of the *mandataire ad hoc*, which is therefore determined and extended, where needed, by the court. The role of the *mandataire ad hoc* is only to make suggestions and to persuade creditors to negotiate with the debtor. He or she has no coercive powers. A *mandat ad hoc* is informal, confidential and purely contractual in nature. The commencement of a *mandat ad hoc* does not impose a stay of payments on the debtor nor a stay of proceedings on creditors. At any moment, the *mandat ad hoc*

proceedings may be converted into conciliation proceedings in order to benefit from the features of the formal approval of the restructuring agreement in conciliation proceedings (see below).

Alternatively, the debtor may seek from the court the appointment of a conciliator in the framework of *conciliation* proceedings to negotiate a voluntary arrangement with key stakeholders, such as creditors, suppliers and possible new sponsors. Conciliation proceedings are also available to an insolvent debtor if the insolvency occurred no more than 45 days before the appointment of the conciliator. The conciliation process is informal, confidential and purely contractual in nature, and does not impose a stay of payments on the debtor nor a stay of proceedings on creditors. If, during the conciliation proceedings, a creditor serves a demand or brings an action against the debtor, the court responsible for the conciliation proceedings has the power to grant the debtor a grace period of up to two years pursuant to article 1244-1 et seq of the French Civil Code (save for claims of tax and social security authorities and institutions). The initial term of the conciliator's mission is determined by the court, within a four-month limit (which can be extended once, for up to one month).

The purpose of both *mandat ad hoc* and *conciliation* proceedings is for the debtor to come to a voluntary arrangement with its creditors that puts an end to its difficulties and ensures the continued operations of its business. Such voluntary arrangement may include a rescheduling or waiver of debts, and sometimes provisions relating to the company's corporate structure (modification of share capital or by-laws, undertaking to sell certain assets, etc). In conciliation proceedings, the conciliation agreement reached may be either:

- certified by the court at the request of all parties to the conciliation agreement, thereby giving it the enforceability of a judgment while keeping it confidential; or
- formally approved by the court at the debtor company's request (homologation). The conciliation then enters the public record.

The formal approval of the conciliation agreement requires the court to be satisfied that the debtor company is not (or as a result of the agreement ceases to be) insolvent; the agreement appears to be such as to ensure the solvent continuation of the debtor's business; and the agreement does not prejudice the interests of those creditors not parties thereto. Such formal approval of the conciliation agreement entails the following specific consequences:

- funds, goods or services made available to the debtor company pursuant to a formally approved conciliation agreement (otherwise than through subscribing to a share capital increase) will benefit from a lien taking priority over most other claims in the event of subsequent safeguard, reorganisation or liquidation proceedings – the 'new money' priority;
- the conciliation agreement will not, in the event of subsequent insolvency proceedings, be void or voidable on the grounds of suspect period rules (see question 39); and
- debt deferrals that may be imposed on creditors during a subsequent safeguard or judicial reorganisation proceedings (see below) may not be imposed with respect to claims that have received the benefit of the 'new money' priority.

If the debtor company fails to perform its obligations under the conciliation agreement, any party to the conciliation agreement may request the court to terminate it. Likewise, the opening of safeguard, reorganisation or liquidation proceedings against the debtor company results in the termination of the conciliation agreement.

The following restriction applies with respect to the *mandat ad hoc* and *conciliation* proceedings: any contractual provisions which, as a result solely of the opening (or a request for the opening) of *mandat ad hoc* or *conciliation* proceedings, would restrict the debtor's rights or increase its obligations, will be deemed to be null and void.

### Safeguard proceedings

The legal representatives of a company that is not yet insolvent and that experiences difficulties that it cannot overcome may apply to the court for the opening of solvent reorganisation proceedings, called safeguard proceedings. The judgment commencing safeguard proceedings opens a six-month 'observation period' (renewable for up to a total maximum period of 18 months) during which the company will negotiate with its creditors a rescheduling or waiver of debts that arose prior to the start

of the safeguard proceedings in the framework of a safeguard plan. The court will appoint a judicial administrator to supervise or assist the debtor company's management in the drawing up of the safeguard plan and a creditors' representative in charge of collecting statements of claims and verifying the debtor's liabilities. Members of the creditors' committee may also present their own alternative safeguard plan.

Safeguard proceedings are listed among insolvency proceedings within the meaning of the EU Insolvency Regulations.

During the observation period, the debtor company enjoys a stay of payments and proceedings, as set out in question 15.

The safeguard plan is drawn up and possibly approved as set out in question 23.

Expedited safeguard proceedings (accelerated safeguard proceedings or financial accelerated safeguard proceedings) may also be opened following conciliation proceedings, as described in question 24.

### Reorganisation proceedings

A debtor company that is insolvent must apply for the opening of insolvency proceedings within 45 days of the occurrence of insolvency, unless it has requested the appointment of a conciliator or the opening of liquidation proceedings (see question 9).

If the court considers that the business may be continued as a going concern, it will order a two-month 'observation period' that can be extended up to a total maximum period of 18 months during which a court-appointed judicial administrator will investigate the affairs of the debtor and make proposals for the reorganisation of its business.

At the end of the observation period, the court will make an order either for the continuation of the debtor's operations by way of a reorganisation plan (the features of which are similar to those of a safeguard plan; as in the case of safeguard proceedings, members of the creditors' committee may also present their own alternative reorganisation plan) or the sale to a third-party purchaser of its assets as a going concern by way of a sale plan.

The reorganisation plan is drawn up and possibly approved as set out under question 23. Features of a sale plan are set out in question 18.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

##### Out-of-court restructuring and safeguard proceedings

Under French law, creditors cannot request the appointment of a *mandataire ad hoc* or a conciliator or request the court to order the commencement of safeguard proceedings.

##### Reorganisation proceedings

Any unpaid creditor may file an application for the commencement of reorganisation proceedings against the debtor. The creditor must show that it has already tried to obtain payment of its debt, and that the debtor is insolvent according to the French insolvency test (see question 1). Reorganisation proceedings can also be started at the initiative of the public prosecutor.

Effects of involuntary reorganisation proceedings are identical to those of reorganisation proceedings opened at the request of the debtor company itself.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Insolvency proceedings must be commenced if the debtor is insolvent (see question 1).

The managing directors of the debtor company are required to file for insolvency proceedings (whether in the form of reorganisation or liquidation proceedings) within 45 days of the date of insolvency, unless they have asked the court to appoint a conciliator (see question 11).

If the managing directors of the debtor company fail to file for insolvency within the required time period, they can be held personally liable in tort for the whole or part of the company's debts, since failing to apply for insolvency proceedings can be considered to be an act of

mismangement. The Macron Law has specified that these provisions will only apply if the failure to file for insolvency proceedings within the required time period is intentional.

If a company carries on business while insolvent, certain transactions entered into and certain payments made by the company may be declared void by the court during subsequent insolvency proceedings – see question 39 with respect to the ‘suspect period’.

### Doing business in reorganisations

- 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor’s business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

#### Out-of-court restructuring

There is no restriction on the conduct of the debtor’s business during the course of *mandat ad hoc* or *conciliation* proceedings except to the extent that restrictions are provided for by the agreement entered into with the creditors.

There are no specific provisions relating to supervision of the business of the debtor while the voluntary arrangement entered into with creditors is in force. The creditors must ask for the termination of the voluntary arrangement in the event that the debtor does not comply with its duties under the arrangement, if any.

See question 16 with respect to the ‘new money’ priority under conciliation proceedings.

#### Safeguard and reorganisation proceedings

During the observation period of safeguard and reorganisation proceedings, the debtor’s management usually remains in charge. In safeguard proceedings, the court-appointed judicial administrator is tasked with either overseeing or assisting the management of the debtor’s affairs. In reorganisation proceedings the judicial administrator is tasked with assisting the management or, in rarer cases, taking over the management.

The debtor continues its operations while preparing the restructuring proposals to be submitted to its creditors. The conduct of the debtor company’s operations is, however, affected by the key effects of the opening of the proceedings, which include the following:

- the debtor is prevented from making payments in respect of any debts incurred prior to the judgment opening the safeguard or reorganisation proceedings;
- all actions and proceedings against the debtor are stayed insofar as they relate to the payment by the debtor of a sum of money, or the termination of a contract for payment default (see question 15);
- secured creditors are not entitled to enforce their security interests over the debtor’s assets;
- no further security may be granted over the debtor’s assets; and
- all transactions outside of the ordinary course of business, including the disposal of assets, must be authorised by the insolvency judge.

Finally, claims that come into existence after the commencement of the safeguard or reorganisation proceedings and that are incurred for the purpose of the proceedings, or in exchange for goods or services provided to the debtor during the observation period, must be paid on their due date. Failing timely payment, they enjoy a priority (known as the ‘post-filing claim’ priority) that will take priority over most other claims (see question 33).

### Stays of proceedings and moratoria

- 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

#### Safeguard and reorganisation proceedings

Secured and unsecured creditors are subject to a stay of proceedings during the observation period, insofar as they relate to the payment

by the debtor of money, or to the termination of a contract for payment default. Therefore, secured creditors cannot foreclose during the observation period.

In addition, all proceedings against the debtor that were begun before the court decision ordering the start of the safeguard or reorganisation proceedings are stayed. They may only continue during the safeguard or reorganisation proceedings for the purposes of fixing the amount of the creditor’s claim.

Proceedings may only be commenced during safeguard or reorganisation proceedings if they concern the payment of sums of money due by the debtor after the commencement of the insolvency proceedings for the purpose of the proceedings or in exchange for goods or services provided to the debtor during the observation period.

#### Liquidation proceedings

During the course of liquidation proceedings, most secured and all unsecured creditors are subject to a stay of proceedings in conditions similar to those applicable to the stay of proceedings in safeguard and reorganisation proceedings.

### Post-filing credit

- 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

#### Mandat ad hoc or conciliation proceedings

During *mandat ad hoc* or *conciliation* proceedings, a debtor may obtain secured or unsecured loans or credit.

In addition, in conciliation proceedings only, new financing granted to the debtor company (other than by way of equity) under a conciliation agreement formally approved by the court (see question 11) will enjoy priority over most other claims, with the exception of the ‘super-privileged’ claim of employees covering all outstanding claims of employees in relation to the 60 days of work before the commencement of the insolvency proceedings (this does not apply in safeguard proceedings as the debtor is deemed solvent) and the insolvency expenses, in the event that insolvency proceedings are subsequently commenced against the debtor (the ‘new money’ priority).

#### Safeguard and reorganisation proceedings

During the observation period of safeguard or reorganisation proceedings (see question 11), a debtor may obtain new financing subject to such new credit being authorised by the insolvency judge and to the extent that it is necessary to the operations of the debtor company during the observation period.

The priority given to such credit depends on whether a liquidation or a reorganisation, through a sale or a reorganisation plan, is ordered by the court at the end of the observation period. As a rule, such authorised new credit granted to the debtor after the opening judgment take priority over most all pre-filing debts (with the exception of the super-privileged claim of employees, the insolvency expenses and the new money priority). However, in the event of a liquidation, such financing will rank after claims secured by security interests over immoveable property as well as special security interests over moveable property that entail a retention right for the creditor (see question 33).

### Set-off and netting

- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

If the creditor and the debtor have reciprocal receivables that arose prior to the opening judgment, set off is automatic.

Set-off may occur post-filing only if the two debts are unquestionable, of a fixed amount, due and linked. Debts are linked when they share a high degree of ‘commonality’. Such ‘commonality’ can result from the following situations: the debts arise from a single contractual relationship; or the debts do not arise from a single contractual relationship but share a sufficient economic ‘link’.

The restrictions set out above do not apply to close-out netting provisions under financial arrangements covered by Directive 2002/47/EC of the European Parliament and of the Council of 6 June 2002 on

financial collateral arrangements, as implemented in French law by Ordinance No. 2005-171 of 24 February 2005 (article L211-36 et seq of the French Monetary and Financial Code).

### Sale of assets

**18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

#### Conciliation proceedings

The conciliator may upon request by the debtor and after consultation with the creditors, arrange a partial or total sale of the business that could be subsequently implemented in the context of further safeguard, reorganisation or liquidation proceedings.

#### Safeguard proceedings

During the observation period of safeguard proceedings (see question 11), the debtor is generally permitted to sell its assets in the ordinary course of business. Disposals out of the ordinary course of business require the authorisation of the insolvency judge.

Safeguard proceedings are designed to allow the debtor company to restructure and to continue its operations. Accordingly, a safeguard plan cannot provide for the sale of all of the debtor company's assets. However, during the observation period or as part of the safeguard plan, the court may make an order for the sale of certain assets, either on a piecemeal basis or as a going concern if such assets form an autonomous branch, provided that the debtor company can continue its operations. If the court orders the sale of a branch, it will occur pursuant to the rules applicable to the sale plan (see below).

#### Reorganisation proceedings

During the observation period of reorganisation proceedings (see question 12) the debtor is generally permitted to sell its assets in the ordinary course of business. Disposals out of the ordinary course of business require the authorisation of the insolvency judge.

At the end of the observation period, when the debtor company proves unable to draw up a reorganisation plan providing for the continuation of its operations, the court may approve the transfer to a third party of all or part of the assets as a going concern by way of a sale plan (see below).

#### Liquidation proceedings

If the court orders the liquidation of the debtor's assets, a liquidator is appointed and the debtor is divested of all rights pertaining to the disposal of assets.

The role of the liquidator is to collect and liquidate all the debtor's assets with a view to maximising proceeds. The debtor's business can be sold as a whole or in part in the framework of a sale plan (see below) or its assets may be sold on a piecemeal basis either at public auction or by private sale.

#### Sale of assets by way of a sale plan

A sale plan is a restructuring plan that provides for the transfer to a third-party buyer of assets, contracts and jobs of the debtor company. By law, the sale plan must achieve three objectives: the continued operations of the transferred business, the preservation of jobs and the repayment of creditors.

The sale plan is an asset deal and not a share deal. Accordingly, the debts of the debtor do not transfer to the purchaser of the business. The main exception is that financings that were granted to the debtor to acquire assets and that are secured by security interests (pledge or else) over those same assets automatically transfer to the purchaser of the business. Other debts remain with the debtor.

All offers are submitted to the judicial administrator or liquidator, where applicable, who in turn submits them to the insolvency court who will, after having consulted the debtor and the workers' council, select the offer most likely to ensure the continued operations of the business, the highest level of employment and the payment of creditors.

The court may also order that the purchaser will not be authorised to sell the business during a certain period.

In practice, bids for the purchase of the debtor's business must all be sent to the debtor or to the judicial administrator or liquidator by a certain date fixed by the latter. Offers will then be examined by the insolvency practitioner and will be presented to the court with the insolvency practitioner's recommendation as to which offer to approve.

There are no 'stalking horse' bids in the sale plan process. Also, there is no possibility of implementing a proper credit bid since French law does not authorise a creditor seeking to purchase assets from the debtor's estate to make payment of the purchase price by reducing the amount of its claim against the debtor: this would be in breach of the legal ranking of creditors for the distribution of sale proceeds.

Once the sale plan is approved by the insolvency court and the assets are transferred to the purchaser, the court official settles the debtor's liabilities with the available sale proceeds according to the waterfall of claims (see question 33) and the company is dissolved.

### Intellectual property assets in insolvencies

**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

Licences to use IP rights cannot automatically terminate upon the debtor company becoming the subject of safeguard or insolvency proceedings. However, such licence agreements may be terminated during the safeguard or insolvency proceedings like any other agreements if the conditions set out in question 21 below are met.

Once the debtor's agreement with an IP licensor or owner is terminated, for any reason, the judicial administrator cannot continue to use the IP for the benefit of the estate.

### Personal data in insolvencies

**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Use of personal information or customer data in insolvency proceedings

Use of personal information or customer data in insolvency proceedings is permitted as long as this use complies with the statement initially made to the French National Commission for Data Protection and Liberties (CNIL). Indeed, according to Law No. 78-17 on Information Technology, Data Files and Civil Liberties, dated 6 January 1978, a company that intends to process personal information or customer data informs and seeks prior authorisation from the CNIL.

#### Transfer of personal information or customer data to a purchaser *Transfer in France or in a Member State of the European Union*

The transfer of personal information or customer data to a purchaser inside the European Union is generally allowed.

However, if the data process initially implemented has not been declared to and/or authorised by the CNIL, the sale of personal information or customer data shall be held null and void (Cass Com 25 June 2013, 12-17.037).

The transfer of client accounts records held by banks and records related to credit or loan management held by banks to third parties is forbidden (*Délibération CNIL* No. 1980-022, dated 8 July 1980 and *Déclaration* 13 dated 10 August 2016).

#### Transfer outside Europe

Transfer of personal information or customer data outside the European Union is forbidden unless the said transfer is to countries that are considered by the European Commission to offer a sufficient level of data protection. In this case, the insolvent company has to inform the CNIL of the contemplated transfer.

The insolvent company can also request an authorisation from the CNIL to transfer the personal information in cases where:

- the purchaser commits himself or herself to respect Law No. 78-17 by a standard contractual clause; and
- the purchaser adopts the Binding Corporate Rules, which is a code of good practices of a group of companies.

The person concerned has to be informed of the transfer of information to a foreign country.

The transfer of customer data (except for customer data collected by banks, health companies, education institutes and insurance companies) implemented in the above-mentioned cases is allowed and does not need to be declared to the CNIL (*Délibération CNIL* No. 2012-209 dated 21 June 2012, norm 48).

#### Rejection and disclaimer of contracts in reorganisations

##### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

As a rule, unfavourable contracts to which the debtor company is a party cannot be rejected or disclaimed during the observation period of the safeguard or reorganisation proceedings.

However, the judicial administrator may apply to court to terminate an agreement to which the debtor company is a party, provided that the judicial administrator can establish that the termination of the agreement is 'necessary to safeguard the debtor company' and it does not 'excessively prejudice' the other party's rights. In such case, the agreement terminates upon the court's decision.

Once safeguard or judicial reorganisation proceedings have been opened against a debtor, the contractual counterparty may require the judicial administrator to specify whether the contract will be continued or not. The judicial administrator must reply within one month. If he or she does not reply, then he or she is deemed to have refused to continue the contract and such contract is automatically terminated. If, however, the judicial administrator has decided to continue the contract, the original contractual provisions will apply. If, once the judicial administrator has decided to continue the contract, the debtor breaches such contract, the contract will be automatically terminated (unless the contractual counterparty agrees to continue such contract once it has been breached by the debtor). However, if the contractual counterparty is a landlord acting with respect to a lease agreement entered into by the debtor in relation to the premises where its activity is carried out and the debtor breaches such contract, the tenancy may only be automatically terminated after a period of three months starting from the judgment opening the safeguard or reorganisation proceedings. If the breach is remedied within such period, no automatic termination may occur.

#### Arbitration processes in insolvency cases

##### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Insolvency proceedings may not be arbitrated and therefore the court cannot direct the parties to an insolvency dispute to submit it to arbitration. Arbitration proceedings that were commenced before the start of the safeguard, reorganisation or insolvency proceedings may only continue during the safeguard or insolvency proceedings for the purposes of fixing the amount of the creditor's claim and provided that the creditor filed a statement of claim and that the court-appointed creditors' representative, and, as the case may be, the judicial administrator, or the person appointed to supervise the implementation of the plan, have been asked to appear in the arbitration court.

Arbitration proceedings may only be commenced during safeguard or insolvency proceedings if they concern the payment of sums of money due by the debtor after the start of the safeguard or insolvency proceedings. Otherwise, arbitration proceedings are stayed during the safeguard or insolvency proceedings, insofar as they relate to

the payment by the debtor of a sum of money or to the termination of a contract for payment default, and may resume only for the purposes of fixing the amount of the debt owed by the debtor.

#### Successful reorganisations

##### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

###### Safeguard plan and reorganisation plan

The safeguard or reorganisation plan must provide for the continued operations of the debtor company in the long term, the settlement of the debtor's liabilities and the preservation of employment.

For companies with more than 150 employees or with an annual turnover in excess of €20 million, the judicial administrator will be required to organise, for the purposes of negotiating a safeguard or reorganisation plan, two creditors' committees:

- the credit institutions committee, made up of financial institutions, similar entities and any holder of a claim acquired from either such a financial institution, such a similar entity or from any supplier of goods or services; and
- the main suppliers' committee, made up of suppliers of goods and services holding at least 3 per cent of the outstanding amount of trade liabilities.

In addition, all the holders of bonds issued by the debtor, irrespective of whether the bond issues are governed by French or foreign law, will be consulted by the judicial administrator in a bondholder's general meeting. However, no separate bondholder committee is established.

The members of the creditors' committee may also present their own alternative safeguard or reorganisation plan, in addition to the one prepared by the debtor's management. However, bondholders are not members of the creditors' committee and therefore will not be able to also propose such alternative plans.

Proposals made to the creditors' committees and the bondholders' general meeting may include waivers of debts, a rescheduling of debts over a period of up to 10 years, a change of control, a sale of certain business units, and, in limited liability companies, a debt-for-equity swap.

The plan must take into account subordination agreements and may provide for a differentiated treatment of creditors if differences in situations warrant it. Each member of the creditors' committee must inform the administrator of the existence of any subordination agreement, any agreement restricting its vote and any arrangement providing for the total or partial payment of its claim by a third party. The judicial administrator shall then submit to such creditor the method for the computation of its voting rights in the creditors' committee. In the event of a disagreement, the creditor or the judicial administrator may request that the matter be decided by the president of the relevant commercial court in summary proceedings.

Each committee and, where there are bondholders, the bondholders' general meeting will have to approve the plan by a positive vote of their members representing at least two-thirds of the aggregate claims of those who vote (irrespective of whether they are secured or unsecured creditors). In addition, any restructuring involving a change in the capital structure (including a debt-for-equity swap) will require the approval of the company's shareholders. The Macron Law has introduced two procedures in this respect providing for an eviction of the shareholders of an insolvent company under judicial reorganisation proceedings if the following cumulative conditions are met:

- the relevant company under reorganisation proceedings has more than 150 employees or it controls a group of companies with a number of employees exceeding 150;
- the cessation of business of such company would materially adversely affect the national or local economy and the local employment; and
- a change in the share capital structure of the company is the only reliable solution to avoid the aforementioned material adverse effect.

The two options provided by the Macron Law with respect to the eviction of shareholders of such companies are:

- the appointment by the insolvency court of a judicial representative who has the power to vote in favour of a share capital increase of the insolvent company in lieu of the dissenting shareholders (it being specified that such share capital increase may be implemented either by a cash injection or by a debt-for-equity swap); or
- the forced sale in favour of entities that undertake to comply with the reorganisation plan of the shares held by the majority shareholders or the minority shareholders of the insolvent company that have a blocking voting right and who refuse to approve the change in the capital structure of the insolvent company.

If both committees and the bondholders' general meeting approve the safeguard or reorganisation plan, the court then officially approves the proposed plan after checking that it is compatible with the interests of all creditors. This decision will make the plan binding on all the creditors, including members of the committees who did not vote or who voted against the proposals.

The consultation of the committees and the approval of the safeguard or reorganisation plan must occur within six months of the opening of the proceedings. Should the creditors' committees reject the proposals or fail to accept within a six-month period, the consultation of the creditors' committees is terminated and all creditors will be consulted individually (see question 38).

In addition, creditors that are not members of the committees (or all creditors when the company does not reach the thresholds for creditors' committees to be set up) will be consulted in relation to a rescheduling or partial waiver of the debts that arose before the start of the safeguard or reorganisation proceedings. Such creditors may be made subject to a uniform rescheduling of debts over a period of up to 10 years (see question 38), save for creditors benefiting from a 'new money' priority with respect to financing provided in the context of a conciliation agreement that has been formally approved by the court.

#### Sale plan

See question 18.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

French law provides for two types of expedited safeguard proceedings: the accelerated safeguard proceedings and the accelerated financial safeguard proceedings. The common features of these two proceedings are the following:

- prior conciliation proceedings are required in order for the debtor to be able to file for one of these expedited proceedings and a safeguard plan must have been prepared that is likely to be supported by creditors representing a two-thirds majority of the debtor's total indebtedness (either secured or unsecured);
- the criteria for a debtor to be eligible for accelerated safeguard and for accelerated financial safeguard proceedings are: either to produce consolidated financial statements or to have its financial statements produced by a certified accountant, or certified by an auditor, and to meet one of the following thresholds: more than 20 employees, a turnover in excess of €3 million or an aggregate balance sheet in excess of €1.5 million; and
- unlike 'ordinary' safeguard proceedings, the special safeguard proceedings may be opened even if the debtor is insolvent, subject to not having been insolvent for more than 45 days prior to the debtors' request for opening of the prior conciliation proceedings.

The main differences between the accelerated safeguard proceedings and the accelerated financial safeguard proceedings are as follows:

- the safeguard plan must be submitted to:
  - the creditors' committees which in the case of accelerated safeguard will include both the financial institutions committee and the main suppliers committee (which have to be formed regardless of whether the debtor meets the criteria specified in question 23 with respect to the committees in the ordinary safeguard proceedings); and in the case of accelerated financial safeguard will include only the financial institutions committee; and

- the bondholders' general meeting (where there are bondholders); and
- the maximum duration of the accelerated safeguard proceedings is three months, while the maximum duration of the accelerated financial safeguard proceedings is one month (with a possibility for the court to extend the financial safeguard proceedings by one additional month).

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

##### Out-of-court restructuring

Failure to reach an agreement in the framework of mandat ad hoc or conciliation proceedings will, in practice, often result in the start of safeguard or insolvency proceedings if the insolvency test is met (see question 1). Accelerated safeguard or financial accelerated safeguard may also be opened by the debtor after conciliation proceedings if the conditions specified in question 24 above are met.

If a conciliation agreement has been certified or formally approved in the context of conciliation proceedings and the debtor has not complied with its duties under that agreement, the creditors who are party to the agreement may request that the agreement is terminated and that insolvency proceedings are opened if the debtor is insolvent.

##### Safeguard and reorganisation proceedings with creditors' committees

When creditors' committees are set up and the committees fail to approve the draft plan within six months from the opening of the safeguard or reorganisation proceedings or the court does not approve the safeguard or reorganisation plan approved by the committees, creditors are then consulted on an individual basis. In such framework, even if creditors refuse the debtor's proposals, the court may make them subject to a uniform rescheduling of their claims over up to 10 years, with no statutory minimum for the first two annual instalments and a minimum 5 per cent of the total liabilities (principal and interest) from the third instalment, although the repayment of a debt under the safeguard or reorganisation plan cannot start before the original contractual maturity (see question 38). Such debt deferrals, however, may not be imposed with respect to claims benefiting from the 'new money' priority.

##### Safeguard proceedings

At any time during the observation period of the safeguard proceedings or if no safeguard plan is approved by the court by the end of the observation period, the debtor, a creditor or the public prosecutor may request the opening of reorganisation or liquidation proceedings, subject to the debtor company being insolvent, and in the case of liquidation proceedings, the absence of any prospects of recovery.

During the observation period, the debtor company may also request the conversion into reorganisation proceedings if the approval of a safeguard plan is manifestly impossible and if the termination of the proceedings would lead to insolvency in the short term.

If the court approves a safeguard plan and the debtor defaults on its obligations, the court may, after having consulted the Public Prosecutor, terminate the plan and, if the debtor is insolvent, order the opening of reorganisation proceedings or (if there are no prospects of recovery) liquidation proceedings.

##### Reorganisation proceedings

At any time during the observation period of the reorganisation proceedings or if no reorganisation plan is approved by the court by the end of the observation period, the debtor, a creditor or the public prosecutor may request the opening of liquidation proceedings.

If the court approves a reorganisation plan and the debtor defaults on its obligations, the court may, after having consulted the public prosecutor, terminate the plan and, if the debtor is insolvent and if there are no prospects of recovery, order the opening of liquidation proceedings. In the case of a sale plan, the court terminates the plan if the third-party purchaser defaults on its obligations.

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## Insolvency processes

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

Notices informing creditors of the start of insolvency proceedings are sent to all known creditors. In addition, all major decisions taken by the court during the course of the safeguard or insolvency proceedings are published in the Official Gazette for Civil and Commercial Announcements. Other key elements of the proceedings (such as the list of claims acknowledged in the safeguard or insolvency proceedings) are filed with the clerk office of the court and may be accessed by the creditors.

The court-appointed officials (judicial administrator, creditors' representative and liquidator) have various duties to report to the court the conduct of the proceedings, in conditions set out in the French Commercial Code.

A creditor may request to be appointed as a supervisor at the beginning of the proceedings. This will entitle him or her to request all the documents sent to the judicial administrator and the creditors' representative, enabling him or her to be kept closely informed of any developments in the proceedings (see also question 27).

Meetings are held during the safeguard or reorganisation proceedings as part of the consultation process involving creditors' committees and the bondholders' general meeting (see question 23).

No release of liabilities owed by third parties who are not part of the debtor group can be provided for in the reorganisation plan.

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## Enforcement of estate's rights

**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

The creditors appointed by the court as supervisors may bring claims on behalf of the debtor company against third parties if the judicial administrator, liquidator or creditors' representative fail to do so for the benefit of all of the debtor's creditors (eg, a claim on the grounds of mismanagement). The proceeds of actions taken by the supervisors belong to the safeguarded or insolvency estate and the supervisors are not granted any priority in respect of those proceeds.

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## Creditor representation

**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

See questions 23 and 24. In situations where creditors' committees are set up (and, as the case may be, the bondholders' general meeting is convened), their power and responsibility is to vote on the debtor's plan proposal. Members of the creditors' committees (but not the bondholders' general meeting) may also put forward alternative safeguard or reorganisation plans. See also question 23. In practice, given that each creditor's committee and the bondholders' general meeting may be composed of creditors whose interests are not aligned, each creditor, or class of creditors within a committee or in the bondholders' general meeting, usually retains its own advisers. Their expenses must usually be funded by the creditors themselves.

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## Insolvency of corporate groups

**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

When several entities of a group of companies are the subject of safeguard or insolvency proceedings, such proceedings are independent from one another and are not combined for administrative purposes.

However, courts tend to use the criterion of the 'centre of main interests' set out in article 3 of EU Insolvency Regulations to centralise the safeguard or insolvency proceedings of a group of companies before the same court so as to conduct the various proceedings in parallel that may facilitate the coordination of the proceedings and the finding of restructuring solutions. Also, the same judicial administrator or creditors' representative may be appointed with respect to insolvency proceedings opened against companies of the same group. In addition, the Macron Law provides that as of 1 March 2016, the court that has jurisdiction over insolvency proceedings opened against a company that is part of a group of companies will also have jurisdiction over any subsequent insolvency proceedings opened against other companies of the same group. There will be, however, an exception to this rule in cases where one of the companies against which insolvency proceedings are opened at a later stage meets the criteria required for the opening of insolvency proceedings in front of a specialised commercial court – in this situation, any insolvency proceedings already opened by the subsidiaries of such company will be transferred to this specialised commercial court.

The only grounds allowing a court to order the combination of proceedings is where there is a 'commingling of assets' between the parent company and its subsidiaries or when the company subject to insolvency proceedings is held to be a sham. If the court makes a finding of commingling of assets or of the company being a sham, the insolvency proceedings from one company will be extended to the other entity of the group and the assets and liabilities of both companies involved will be pooled for distribution purposes.

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## Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

The debtor that is in an insolvency proceeding has the right to appeal a judgment, within 10 days from the notification of the judgment, where the judgment:

- opens or extends the safeguard, reorganisation or liquidation proceedings;
- converts the liquidation proceeding into reorganisation proceedings;
- declares the debtor insolvent; or
- approves, modifies or terminates a safeguard or reorganisation plan.

The debtor can also appeal the judgment that approves or rejects the sale plan, within 10 days of the said judgment.

Finally, the debtor can lodge an opposition to orders of the insolvency judge (except orders related to the appointment or change of insolvency judge) within 10 days of the notification of the order.

He or she can also appeal orders of the insolvency judge related to:

- the verification and admission of creditor claims;
- the replacement of guarantees;
- cash advances from the Tax Office; or
- the sale of the debtor's goods, when the latter is facing liquidation proceedings.

The creditor requesting the opening of the insolvency proceedings can appeal the judgment opening (only if the creditor challenges the date retained by the court as the date on which the debtor company became insolvent) or refusing to open the reorganisation or liquidation proceeding.

The appellant has an automatic right of appeal: he or she does not have to request an authorisation or post security to proceed with an appeal.

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**Claims**

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

Generally, creditors must file a statement of their claims in the insolvency proceedings within two months (four months if they reside outside mainland France) from the publication of the opening judgment in the Official Gazette for Civil and Commercial Announcements. When the amount of the claim is contingent or unliquidated, the creditor must declare an assessment of the amount of its claim. Unless the creditors' representative challenges the amount of the claim, it will be admitted on the basis of this assessment. Failure to file a claim within these time limits results in the creditor being unable to take part in the subsequent distributions of cash, save for the case where the debtor has filed such claim of the creditor (the debtor having a legal obligation to file a list of all its creditors and the amount of their claims) in which case he is deemed to have acted on behalf of the creditor. Such creditor may ratify the debtor's filing at any time until the court has made a final decision accepting or rejecting the claim. Also, the court may, in certain circumstances (including the case where the debtor has failed to include such claim in the list of claims it has filed), authorise a creditor to file a claim after the expiry of the original deadline mentioned above.

The creditors' representative will give notice to those creditors whose debts are protected by a registered security interest (essentially mortgages and pledges) or by leasing agreements, at the start of the proceedings. Other creditors (in particular the unsecured creditors) will learn about the start of the insolvency proceedings from the notice published in the Official Gazette.

The creditors' representative will then verify the filed statements of claims. The debtor may submit observations with respect to such claims within 30 days. If the debtor does not submit such observations in the deadline it is barred from subsequently challenging such claims. Any creditor may also challenge a claim made by another creditor. If a claim is challenged by the creditors' representative, the debtor or a creditor, the case will be brought before the court, which will decide whether to accept or reject the claim. Such a decision may be challenged before the Court of Appeal within 10 days of the notification of the decision by the clerk office of the court.

As a rule, a creditor remains free to assign its claims to a third party after the opening of safeguard or insolvency proceedings. However, such transfer must be brought to the judicial administrator's attention by registered post to ensure that the assignee is invited by the judicial administrator to take part in the creditors' committees or the bondholders' general meeting, where applicable. A claim acquired at a discount may be subsequently enforced for its full face value.

Accrual of interest is suspended during safeguard, reorganisation and liquidation proceedings, except with respect to loans providing for a term of at least one year or contracts providing for a payment that is deferred for at least one year. Also, interest can no longer be compounded during the observation period.

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**Modifying creditors' rights**

**32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

In the framework of a safeguard or a reorganisation plan, the plan must take into account the subordination agreements entered into prior to the commencement of the proceedings (see question 23). In the framework of a sale plan or liquidation proceedings, the rank of a creditor's claim is determined by law (see question 33).

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**Priority claims**

**33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Priorities are determined by many different laws and cannot be set out definitively. However, apart from employee-related claims, priorities in liquidation proceedings are generally as follows:

- costs of the insolvency proceedings;
- the 'new money' priority (for new financing, providing of new goods or services, granted under a formally approved conciliation agreement (see question 11));
- claims secured through security interests over immovable property, specific security interests over moveable property, in particular security interests to which a retention right is attached;
- claims that have arisen after the judgment opening the insolvency proceedings and which are necessary for the conduct of the proceedings (eg, rental payments to maintain the lease of the premises where assets are located until such assets are sold by the liquidator); and
- other claims according to existing priority rules.

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**Employment-related liabilities in restructurings**

**34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

**Employee claims**

Employee claims encompass all unpaid salaries and benefits. Employees are exempt from filing a statement of their claims.

Employees' claims are guaranteed by a national insurance fund called the AGS, funded by employers. The AGS guarantees the payment of the employees' claims up to certain caps in safeguard, reorganisation and liquidation proceedings. For all sums paid to employees, the AGS is then subrogated to the rights of the employees against the debtor company. The AGS will therefore be reimbursed, as the case may be, according to the ranking of the employees' claims (eg, the AGS will be ranked first regarding unpaid wages for the 60 days of work preceding the opening of reorganisation or liquidation proceedings).

**Termination of employment contracts**

In safeguard proceedings, the procedure to terminate employment contracts is the same as outside insolvency proceedings.

In reorganisation proceedings, employees may be made redundant during the observation period if the redundancies are urgent, unavoidable and necessary. The judicial administrator must consult the employees' representatives or works council and inform the labour authorities before submitting a list of positions that the judicial administrator would like to have removed. The insolvency judge must then authorise the dismissals based on such list. The judicial administrator can then make employees redundant in accordance with the list of positions to be removed.

In liquidation proceedings, the liquidator must terminate all employment contracts within 15 days of the date of the judgment ordering the liquidation or at the end of the temporary continuation of the debtor's operations, where applicable. Termination must be preceded by the consultation of the employees' representatives or the works council and the information of the labour authorities.

If the business is sold by way of a sale plan (whether approved in reorganisation or in liquidation proceedings), employment contracts included in the plan approved by the court automatically transfer to the purchaser. Non-transferred employment contracts are terminated by the judicial administrator or liquidator (see question 18).

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**Pension claims**

**35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

In most cases in France, existing employee pension plans or schemes are externalised (ie, an entity independent from the debtor company is in charge of receiving the contributions and then distributing the pension to the employees when they retire). As a consequence, the insolvency of the debtor company has no impact on the pension plans

or schemes. However, in cases where the employee pension plan is internal to the debtor company, as a rule the AGS refuses to guarantee the payment of the pension to the employees, who must therefore file a statement of their claim and will not benefit from any priority ranking. This rule adopted by the AGS is, however, subject to debate, and in at least one decision of the French Supreme Court, dated 25 January 2005, it was considered that the AGS should guarantee payment. This payment will be limited to the maximum amount guaranteed by the AGS (see above at question 34).

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The environmental problems of a company in insolvency proceedings must be controlled by both its managing directors (if they are still in charge of the management of the company) and the insolvency administrator, if it has been granted power to oversee or assist with the management of the company (in safeguard, judicial reorganisation or judicial liquidation proceedings) or by the insolvency administrator if it has taken over the management of the company (in judicial reorganisation or judicial liquidation proceedings). The insolvency administrator must also request an environmental audit during safeguard proceedings or judicial reorganisation proceedings and must ensure that the safeguard or reorganisation plan that is presented to the court takes into account the environmental actions contemplated in such environmental audit.

Liabilities with respect to the environmental problems of a company in insolvency proceedings may be imposed on:

- the debtor's managing directors, by an action for shortfall in the company's assets, which can be brought in liquidation proceedings on the ground that such directors have, by acts of mismanagement, contributed to a shortfall in the company's assets;
- the insolvency administrator, but only in some limited circumstances such as not having taken some urgent measures necessary to ensure the safety of the site (ie, measures needed to prevent an immediate and proven risk for safety and public health) with respect to the pollution caused by the company in insolvency proceedings;
- the shareholders, by an action which has been introduced in French law (article L512-17 of the French Environmental Code) by the Grenelle 2 law (Law No. 2010-788 of 12 July 2010), which provides that a parent company may be required by a court to bear all or part of the remedial costs incurred in relation to a polluting activity by one of its subsidiaries which is in liquidation proceedings if such parent company has committed a fault having caused a shortfall in the insolvent subsidiary's assets;
- the insurance companies, against whom the victims of the pollution caused by the company in insolvency proceedings have a direct action; or
- the Environmental Agency, ADEME, if all other liable persons are unknown, insolvent or defaulting.

Also, in certain circumstances the victims of pollution caused by an insolvent company can be indemnified by specific national or international compensation funds created in relation to certain types of pollution.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Generally, no further claims may be brought against the debtor once liquidation proceedings are closed.

In addition, subject to limited exceptions, the purchaser of the debtor's assets in the framework of a sale plan purchases the assets free from any liens or past liabilities (see question 18).

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

##### Safeguard proceedings

Subject to their acceptance in the safeguard proceedings, pre-filing liabilities are repaid in accordance with the terms and conditions of the safeguard plan approved by the court with the profit generated by the continued operations of the business and, where applicable, the proceeds of the sale of certain assets of the debtor. Debts incurred after the start of the proceedings must generally be paid when due (see question 14).

When the creditors' committees and, where applicable, the bondholders' general meeting, have rejected the restructuring proposals made by the debtor or by members of the creditors' committees (see question 23), the court cannot impose a waiver of debt on creditors. However, it can impose a 'term-out' by which claims are to be repaid in annual instalments over a maximum of 10 years, save for claims benefiting from a 'new money' priority. The first annual instalment is payable at the latest 12 months after the court order imposing the rescheduling of debts, with no statutory minimum for the first two instalments and a minimum 5 per cent of the total liabilities (principal and interest) from the third instalment, although the repayment of a debt cannot start before the original contractual maturity. The same rules apply for safeguard proceedings where no creditors' committees are set up and for creditors that are not members of creditors' committees.

If the debtor does not comply with the obligations provided for by the safeguard plan, the court may order the termination of the plan. If the debtor is insolvent according to the French insolvency test (see question 1), such termination may result either in the start of reorganisation proceedings or liquidation of the debtor if there are no prospects of recovery (see question 25).

##### Reorganisation proceedings

At the end of the observation period, the court will order either a reorganisation plan or a sale plan.

The rules set out above for distributions made under a safeguard plan also apply to the reorganisation plan. If the debtor does not comply with the obligations provided by the reorganisation plan, the reorganisation plan may be terminated by the insolvency court and liquidation proceedings may be opened.

A sale plan is implemented pursuant to the provisions set out in the French Commercial Code regarding liquidation proceedings. If the court approves a sale plan, the price paid by the third-party purchaser will be allocated to the repayment of the debts pursuant to the priority rules set out in the French Commercial Code (see question 33). In this case, distribution will occur once sale proceeds have been collected and after the statements of all claims have been verified and are final.

##### Liquidation proceedings

In liquidation proceedings, distributions are made by the liquidator according to priority rules (see question 33) as sale proceeds are collected and after the statements of all claims have been verified and are final.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

When a debtor is the subject of insolvency proceedings (whether reorganisation proceedings or liquidation proceedings), the insolvency court can annul certain transactions entered into, and certain payments made, by the debtor during the 'suspect period'. The suspect period is defined as the period between the date on which the debtor is deemed to have become insolvent, as determined by the insolvency court, and the date on which insolvency proceedings are opened. The date of the debtor's insolvency cannot be set earlier than 18 months before the judgment opening the insolvency proceedings or before the judgment formally approving a conciliation agreement (see question 11).

The rationale behind the possibility of setting aside such acts and transactions made during the suspect period is to restore the estate of the debtor and to cancel advantages granted by an insolvent debtor to

one of its creditors, to the detriment of the collective interest of all its other creditors.

The French Commercial Code provides for a list of transactions and acts that are set aside by the court when made during the suspect period. This includes in particular:

- disposals of assets without consideration;
- contracts that impose unduly onerous obligations on the debtor;
- payments of debts before they are due;
- payments that are not made: in cash, through specific negotiable instruments, by wire transfer, through Dailly assignments or payments that are made other than by normal commercial means;
- cash collateral ordered by a court (under article 2350 of the French Civil Code), unless it has been ordered by a court decision having the force of *res judicata*;
- mortgages and pledges granted by the debtor over its moveable or immovable property that secure debts entered into prior to the granting of such security interests; and
- transfers of assets and rights into a trust, unless such transfer has been made in order to secure a debt entered into in the same time as such transfer of assets.

In addition to the above, French courts have a discretionary power to set aside any transaction if the two following conditions are met:

- the transaction was entered into during the suspect period; and
- the other party knew that the debtor was already insolvent (according to the insolvency test described in question 1) when it made the payment or entered into the transaction.

If an act or transaction is annulled by the court, the creditor will be deprived of its rights and will have no claim under the act or transaction that has been declared null and void.

A claim to annul a payment made, or a transaction entered into, during the suspect period may be brought by the judicial administrator, the creditors' representative, the liquidator or the public prosecutor.

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#### Proceedings to annul transactions

- 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

See question 39.

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#### Directors and officers

- 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

Managing directors (whether officially appointed or *de facto* directors) of an insolvent company may be held personally liable for the debts of the company if they are found to have mismanaged the company's business – prior to the opening judgment of liquidation proceedings – and if their mismanagement contributed to the shortage of assets in the debtor company.

Criminal and professional sanctions may also apply to corporate officers and directors in certain circumstances.

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#### Groups of companies

- 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

As a general rule, under French law a company is a separate legal entity from other companies of the same group, including its shareholders and subsidiaries. As a result, its assets cannot be affected by insolvency proceedings commenced against other companies, even if these companies belong to the same group. Nevertheless, the corporate veil may be lifted and insolvency proceedings commenced against one company may be extended to another (even if such other company is not insolvent) either on the ground that the debtor company is held to be a fictitious legal entity or that the assets and liabilities of the parent

company and those of its subsidiary as so intertwined that they should in fact be considered to be one single entity.

#### Extension on the ground that the debtor company is a fictitious legal entity

Case law considers that a company is a fictitious legal entity where a separate legal entity exists in form only (ie, the company has no autonomy and does not exist as an independent entity despite the existence of an independent legal structure or has been set up fraudulently, or both). The courts, however, only rarely extend insolvency proceedings commenced against one company to another company on the ground that the company is a fictitious legal entity.

#### Extension on the ground of mix-up of assets and liabilities

A French court may only hold that there has been a mix-up of two companies' assets and liabilities if it finds that two conditions, theoretically alternative but most of the time used cumulatively, are met: there must be a commingling of accounts and abnormal financial streams (being analysed by case law as systematic transfers of assets or of services without consideration).

This French rule, however, cannot be applied with respect to a company having its registered office in another EU state, according to a decision of the EU Court of Justice dated 15 December 2011 (*Rastelli Davide e C Snc v Jean-Charles Hidoux C-191/10*), which was confirmed by a decision of the French Supreme Court dated 10 May 2012. According to these decisions, insolvency proceedings opened against a French company with its COMI in France cannot be extended on the ground of the French rule mentioned above to a company having its registered office (and its COMI) in another EU state.

See also question 36 with respect to the specific action relating to environmental liabilities whereby a parent company may be required by a court to bear all or part of the remedial costs incurred in relation to a polluting activity of one of its subsidiaries that is in liquidation proceedings.

There are no provisions under French law allowing a court to order a distribution of group company assets *pro rata* without regard to the assets of the individual corporate entities involved.

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#### Insider claims

- 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

French insolvency law does not specifically address this issue; however, all claims are reviewed and checked by the creditors' representative and the court has the power to reject such claims if deemed invalid. See question 39 with respect to transactions that can be annulled if entered into during the suspect period under certain circumstances, in particular, contracts that impose unduly onerous obligations to the debtor and transactions entered into with a party that had knowledge of the fact that the debtor was already insolvent when it has entered into the transaction.

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#### Creditors' enforcement

- 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

Once safeguard judicial reorganisation or liquidation proceedings are started against a debtor, its assets may not be seized (since there is an automatic stay of proceedings in place). This is without prejudice to the rules provided under the EU Insolvency Regulations for assets located in a member state other than France on the date of the opening of the safeguard or insolvency proceedings.

Notwithstanding the above, a creditor that legitimately retains possession of one of the debtor's assets may obtain full payment of its claim in exchange for the release of the asset (subject to the asset being necessary to the debtor's operations). In addition, a creditor secured by a pledge over one of the debtor's assets may, under certain conditions, be granted full ownership of the said asset in payment of its debt in the event of liquidation proceedings.

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**Corporate procedures**


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**45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

A company may be liquidated and wound up outside the scope of insolvency proceedings and outside court proceedings if it is in a position to repay all its debts.

In this case, the shareholders or the court will appoint a liquidator who will be in charge of the distribution of the company's assets and payment of the company's debts. When all distributions have been made and debts paid (which must be done within three years from the start of the liquidation), the shareholders will decide in a general meeting whether the liquidation process should be closed. The corporate entity will only cease to exist when the liquidation is completed. In this event, the liquidator will request that the company be removed from the Trade and Companies' Registry.

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**Conclusion of case**


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**46 How are liquidation and reorganisation cases formally concluded?**

Out-of-court restructurings are formally concluded when:

- parties have agreed on a restructuring agreement (whether in mandat ad hoc or conciliation proceedings), if no approval from the court is required by the parties;
- the conciliation agreement has been either certified by the presiding judge of the court or formally approved by the court (see question 11); or
- at the end of a maximum five-month period of the opening of conciliation proceedings if no agreement has been reached by the parties (see question 11).

Safeguard and reorganisation proceedings are formally concluded upon the approval of the safeguard or reorganisation plan. In addition, once the safeguard or reorganisation plan has been fully implemented, the court official in charge of supervising the implementation of the plan will draft a report confirming the completion of the plan to the court.

Liquidation proceedings are formally concluded when all debts have been repaid, the liquidator has been able to obtain sufficient proceeds in order to repay all debts, the continuation of the liquidation proceedings is impossible due to a shortfall of assets or the continuation of liquidation proceedings is considered to be no longer justified due to difficulties in selling the remaining assets.

If the debtor is in ongoing judicial proceedings, the insolvency court may, however, close the liquidation proceedings, subject to a representative being appointed that must continue the ongoing judicial proceedings on behalf of the liquidated debtor and allocate the proceeds obtained from such proceedings to the creditors of the liquidated debtor.

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**International cases**


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**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Rules concerning insolvency proceedings of companies with their COMI located within the European Union (other than Denmark) are contained in the EU Insolvency Regulations. The EU Insolvency Regulations provide for an automatic recognition in France of insolvency proceedings carried out in another EU member state (save for Denmark). For further information please refer to the EU chapter.

Outside the scope of the EU Insolvency Regulations, insolvency proceedings begun in another country have limited effects in France, until they are officially recognised through an exequatur judgment and are made enforceable in France. Up until then, debtors can be the subject of enforcement measures or insolvency proceedings in France.

Once the foreign insolvency proceedings are recognised in France, the foreign insolvency rules apply. The company's assets and business in France are handled in accordance with these rules. Payments made or transactions entered into during the suspect period defined by the foreign law, prior to the start of the insolvency proceedings, can be challenged. The foreign insolvency proceedings are expected to produce their full effects.

The adoption of the UNCITRAL Model Law on Cross-Border Insolvency has been discussed but, for the time being, no steps have been taken to implement it in France.

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**COMI**


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**48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

French courts are using the technique of a 'body of corroborating evidence' in order to determine the COMI of a debtor company or group of companies. The cumulative effect of several of the following pieces of evidence is used:

- the nationality and residence of the directors of the company;
- the location of the board meetings of the company;
- the location from where the strategic and operational management of the company is performed;
- the place where the main negotiations concerning the company are led;
- the location of the main creditors of the company;
- the location of the main assets of the company;
- the law governing the main contracts of the company;
- the place from where the supplies of goods are produced;
- the place where the strategic, operational and financial divisions of a group of companies are located; and
- the location of the majority of the employees of the company or group of companies.

There is, however, no definite line or principle followed or applied by the French courts in their analysis relating to the location of the COMI and the absence of established case law means that French courts may not necessarily apply the same criteria from one court to another when examining similar cases.

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**Cross-border cooperation**


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**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

See question 47 with respect to the recognition in France of foreign insolvency proceedings.

The EU Insolvency Regulations provide for cooperation between an insolvency practitioner appointed in main insolvency proceedings opened in an EU member state and an insolvency practitioner appointed in secondary proceedings opened in another EU member states (article 31 of the 2000/1346 EU Insolvency Regulation and article 41 of the 2015/990 EU Insolvency Regulation).

Judicial administrators can enter into insolvency protocols or other arrangements with foreign courts, although it is not common practice in France and, in any event, it will be decided on a case-by-case basis. To our knowledge, there have been limited examples of such process. One example of a protocol can be found in the *Sendo International* case, where main insolvency proceedings had been commenced in the United Kingdom against the company *Sendo International* and secondary proceedings had been opened in France. The liquidators of both proceedings had entered into a protocol intended to establish a practical modus operandi in order to enable effective cooperation between the two insolvency proceedings. This protocol notably provided how to proceed with the statements of claims, the debtor's assets as well as the liquidation proceeds (Commercial Court of Nanterre, 29 June 2006, *Sendo International*). A more recent example can be found in the *Nortel*

restructuring where insolvency protocols have been signed between the administrators appointed in the main proceedings (administration) in England with respect to the French Nortel companies and the judicial administrator appointed in the French secondary proceedings.

French courts may refuse to recognise foreign insolvency proceedings based on the following grounds: with respect to EU insolvency proceedings, a conflict with the French international public policy (article 26 of the 2000/1346 EU Insolvency Regulation and article 33 of the 2015/848 EU Insolvency Regulation) or a limitation of personal freedom or postal secrecy (article 25, paragraph 3 of the 2000/1346 EU Insolvency Regulation) and, with respect to other foreign insolvency proceedings (outside the EU), if one or more conditions for exequatur are not met (see question 47 with respect to the exequatur of foreign insolvency judgments). However, there are very rare cases where foreign judgments have not been recognised.

#### **Cross-border insolvency protocols and joint court hearings**

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

See question 49.



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# Germany

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

In principle, the German Insolvency Act governs all bankruptcies and judicial reorganisations in Germany. As regards the restructuring and orderly winding up of financial institutions, the prerequisites and proceedings are primarily stipulated in the Law on Bank Restructuring dated 9 December 2010 (see questions 3 and 5). Furthermore, there are a number of special provisions in the German Banking Act granting certain rights and responsibilities to the German Federal Financial Supervisory Agency (FSA) in the (threatened) insolvency of a financial institution. For example, the FSA can impose a temporary moratorium.

In general, the German Insolvency Act specifies two different criteria for establishing insolvency: illiquidity; and, if the debtor is a legal entity (limited liability company, stock corporation, etc) or a (limited liability) partnership that has solely legal entities as (general) partners, over-indebtedness.

### Illiquidity

According to the Insolvency Act, a debtor is illiquid when it is unable to pay its debts as they fall due. A company is deemed to be illiquid if it has ceased making payments. The German Federal Supreme Court decision of 24 May 2005 (IX ZR 123/04) has, however, set out the following qualifications:

- if it can reasonably be expected that the debtor will meet its payment obligations within no more than three weeks from their due date, the company is not considered illiquid;
- if the liquidity shortfall amounts to less than 10 per cent of all due payment obligations the company is only considered illiquid if the shortfall is likely to increase to more than 10 per cent in the near future; and
- if the liquidity shortfall amounts to 10 per cent or more of the due payment obligations illiquidity is assumed, unless there is a high likelihood that the shortfall will soon be covered completely, or almost completely, and the creditors can be reasonably expected to wait. Accordingly, a mere temporary interruption of payments will not constitute illiquidity.

### Over-indebtedness

In general, a company will be regarded as being over-indebted whenever the company's total liabilities (including accruals) exceed its total assets (including hidden reserves, which can be taken into account). Until 17 October 2008, where there was a predominant probability that the company's business could be continued, the evaluation of the company's assets was permitted to be undertaken on a going-concern (rather than liquidation) basis. If such valuation on a going-concern basis (and the consideration of hidden reserves) still resulted in a negative net asset value, the company had to file for insolvency (notwithstanding the predominant probability of a continuation of its business). With effect as of 18 October 2008, as a consequence of the financial crisis, the Insolvency Act was modified so that a company is generally no longer regarded as being over-indebted when there is a predominant likelihood that the company's business can continue. This modified over-indebtedness test was supposed to only be in force for an

interim period until 31 December 2013. However, in December 2012 the German legislator decided to adopt this modified legal definition of over-indebtedness for an indefinite period.

### Threatened illiquidity

In addition, the Insolvency Act establishes the concept of 'threatened illiquidity'. This gives the debtor (but not the creditors) the right to initiate a reorganisation or liquidation under the Insolvency Act when the company's illiquidity is imminent (see questions 9 to 13).

The debtor is deemed to be threatened with illiquidity if it is likely to be unable to meet its existing payment obligations when they fall due. This is particularly the case when it appears that the company is more likely to become illiquid than to recover. In practice, a company threatened by illiquidity is usually also over-indebted.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The lower court of the district in which a state court is located has exclusive insolvency jurisdiction for that district.

If the centre of the debtor's business activity is located in another district, the insolvency court of that district will have exclusive local jurisdiction. If more than one court has jurisdiction, the court in which the application for commencement of the insolvency proceeding was first filed will have exclusive jurisdiction.

The competent insolvency court has jurisdiction to deal with all matters connected with the insolvency proceeding. Among other things, the insolvency court can suspend creditors' attempts to enforce against the debtor's assets (save for real property). The position is different where there is a judicial execution of the debtor's real property. The execution in that case can only be temporarily suspended by the court having jurisdiction over the execution, and not by the insolvency court.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

In principle, insolvency proceedings may be commenced by or against any natural or legal person. An unincorporated association that otherwise has no separate legal personality will be deemed to be a legal person. Insolvency proceedings cannot, however, be commenced against any legal entity that is subject to state supervision, if the law of the respective state so provides.

Furthermore, the Law on Bank Restructuring (see questions 1 and 5) provides for specific rules concerning the restructuring and orderly winding up of financial institutions.

In principle, the insolvency proceedings involve all of the assets owned by the debtor on the date when the insolvency proceedings are opened and those acquired by the debtor during the insolvency proceedings. However, there are certain exceptions as regards the assets of natural persons that cannot be enforced over or form part of the

insolvency. From a practical point of view, this exemption does not affect corporate insolvencies.

#### Public enterprises

##### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

German insolvency law does not provide for specific procedures for government-owned enterprises. Hence, the provisions under the German Insolvency Act also apply for such enterprises.

However, insolvency proceedings cannot be commenced against the federal government or a state government, or any legal entity that is subject to state supervision, if the law of the respective state so provides (see also question 3).

Creditors of insolvent public enterprises have the same remedies as creditors of insolvent non-public enterprises (as to the remedies of unsecured creditors, see question 8).

#### Protection for large financial institutions

##### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

In view of the worldwide financial crisis, the German legislator passed, among others, the Law on Bank Restructuring, which became effective on 1 January 2011. The Law on Bank Restructuring provides specific rules concerning the restructuring and orderly winding up of financial institutions. The rationale of the law is that the financial distress of a bank should primarily be rectified by its stakeholders (ie, in particular its shareholders and its creditors). An intervention by the FSA may only be considered if the stakeholders fail to implement adequate restructuring measures and if the stability of the financial system is otherwise at risk.

The Law on Bank Restructuring provides for two restructuring procedures, both of which can only be initiated by the financial institution itself: a recovery procedure and a restructuring procedure. Both procedures provide a framework for a collective negotiated settlement.

The recovery procedure can be initiated by the management of a distressed bank far in advance of a potential insolvency. The recovery procedure may be commenced after the management gives notice of its need for recovery and presents a recovery plan to the FSA. Such plan must outline the measures proposed to recover the bank, but may not impair any third-party rights.

Alternatively, a restructuring procedure may be initiated if the existence of the bank is endangered and if the collapse of the bank would severely affect the stability of the financial system. The restructuring procedure is shaped along the lines of the insolvency plan procedure under the Insolvency Act (see question 23), meaning that creditors of the financial institution form different creditor groups that vote on the restructuring plan (including the possibility of a cram down). Such a restructuring plan may impair shareholder rights and may also provide for a debt-to-equity swap. Beyond this, the restructuring plan may also stipulate the spin-off of certain parts of the financial institution to an existing or a newly established affiliate.

If the stakeholders are not willing to stabilise the financial institution in distress or if the measures taken do not sufficiently allow for a recovery of the institution, so the stability of the financial system is (still) in danger, the FSA is empowered to nominate a special representative who is assigned certain tasks, responsibilities and rights that the FSA considers necessary to recover the financial institution. In addition, the FSA has the power to force a financial institution to transfer its business in whole or in part to another (public or private) bank.

There is no specific restructuring act for insurance companies. It must, however, be noted that there are some special rules for insolvency proceedings over the estate of insurance companies (section 88 et seq of the German Insurance Supervision Act). For instance, if an insurance company becomes insolvent, only the supervising authority may file an application for the commencement of insolvency proceedings.

#### Secured lending and credit (immovables)

##### 6 What principal types of security are taken on immovable (real) property?

The principal types of security devices that are taken on immovable (real) property are as follows.

###### Hypothek

Real property can be charged by way of a *hypothek* (ie, mortgage) as security for payment of a definite sum that equals the secured personal debt. It is not necessary for the creation of a *hypothek* that the owner of the real property is the personal debtor in respect of the claim secured by the charge. The *hypothek* may be certificated or non-certificated. Both forms are registered with the land register, but only the holder of a certificated *hypothek* receives a certificate after registration that enables him to transfer the *hypothek* external to the register by means of written assignment and handing over the certificate.

###### Grundschild

A *Grundschild* (ie, land charge) creates a charge on real property for the payment of a definite sum of money. It differs from a *hypothek* because it does not depend on an underlying personal debt and theoretically may exist without one. In practice, the parties usually agree that the *Grundschild* will not be transferred back to the real property owner until all outstanding sums have been repaid.

#### Secured lending and credit (moveables)

##### 7 What principal types of security are taken on moveable (personal) property?

The principal types of security devices that are taken on moveable (personal) property are:

- retention of title: pursuant to section 449 of the Civil Code, the seller of personal property may retain title over the assets it is selling until the purchase price has been paid;
- fiduciary transfer of assets: a fiduciary transfer of assets is an arrangement pursuant to which a debt is secured on personal property, possession of which is retained by the debtor;
- fiduciary transfer of receivables: a fiduciary transfer of receivables is an arrangement whereby security is granted over receivables owed to the debtor; and
- chattel pledge: a chattel pledge is created by pledging a chattel (or claim) as security for a debt. It is a right in rem to satisfy a claim. A chattel pledge requires that the debtor delivers up possession of the chattel.

In practice, one will often find a combination of these security devices. For instance, suppliers usually supply their products on retention of title terms. However, the terms of supply may entitle the retailer to sell the products in the ordinary course of business, provided that the (future) receivables arising from such sales to customers are assigned to the supplier in advance by fiduciary transfer.

#### Unsecured credit

##### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

An unsecured creditor must first obtain a judgment in respect of its debt. It can then initiate a judicial execution of the debtor's personal or real property. However, these procedures can be very difficult and time-consuming, especially if the debtor contests the creditor's claim. In principle, an attachment could be obtained in advance of a judgment or execution but only where certain strict requirements have been met. An example would be if the enforcement of the judgment would become impossible or considerably more difficult without such a court order.

Foreign creditors in possession of a foreign judgment would have to apply to a German court for recognition of their judgments before bringing steps to enforce it.

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## Voluntary liquidations

### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Generally, a voluntary liquidation may only be implemented in accordance with general corporate procedures if the debtor is able to discharge all its debts or reach an out-of-court settlement with all its creditors.

Under the Insolvency Act, the debtor may (voluntarily) initiate insolvency proceedings under the Insolvency Act when illiquidity threatens (as defined in the Insolvency Act (see question 1)).

Upon the commencement under the Insolvency Act, the debtor is generally divested of the power to dispose of its assets. An insolvency administrator is then appointed by the court. In this context, it should, however, be noted that the Insolvency Act provides for self-administration proceedings that give the debtor the opportunity to continue to manage and administer the insolvency estate, subject to the supervision of a custodian who usually is an insolvency practitioner. However, self-administration proceedings are not designed to initiate a voluntary liquidation but rather a voluntary reorganisation (see also questions 11 and 14).

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## Involuntary liquidations

### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Insolvency proceedings can only be commenced by the presentation of an application. An application may be presented by a creditor if the creditor can establish that the debtor is unable to pay its debts as they fall due or, in the case of a legal entity or a (limited liability) partnership that has only legal entities as (general) partners, that the entity is over-indebted (as defined in the Insolvency Act (see question 1)). If the creditor's application is well founded, the insolvency court will then give the debtor an opportunity to be heard.

Upon the commencement of the insolvency proceedings, the insolvency administrator immediately takes possession of, and administers, all assets that constitute the insolvency estate. Moreover, the debtor's management will be subject to a positive duty to provide information.

Once the administrator has taken possession of the debtor's assets, he or she is required to prepare a list of the assets comprising the insolvency estate, in which the value of each object is stated. The administrator must also prepare a list of all creditors whose names appear in the books and papers of the debtor, or whose identities are revealed by other statements of the debtor, or who assert their claims in the course of the proceeding. In addition, the administrator is obliged to prepare a statement of affairs. Once all the assets of the estate have been realised and the final distribution has taken place, so that the insolvency proceedings will be closed, the legal entity or partnership will be erased from the commercial register.

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## Voluntary reorganisations

### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

If the debtor is a legal entity or a (limited liability) partnership with legal entities only as (general) partners, and it is established that the debtor cannot pay its debts as they fall due or the debtor is over-indebted (as defined in the Insolvency Act (see question 1)), the managing directors of the debtor are compelled by German law to apply for the commencement of insolvency proceedings without undue delay and, in any event, at the latest within three weeks from the date on which the company became insolvent. In addition, the Insolvency Act gives the debtor (but not the creditors) the ability to initiate a reorganisation when illiquidity threatens (as defined in the Insolvency Act (see question 1)). In both insolvency or pending illiquidity, the debtor can combine the application for the commencement of an insolvency proceeding with an application for self-administration proceedings and the submission of a reorganisation plan (the 'pre-packaged' plan). Furthermore, if (merely) an over-indebtedness or a threatening illiquidity (or both) has occurred (as defined in the Insolvency Act (see question 1)), section 270b of the Insolvency Act provides for an early self-administration procedure (the 'protective shield procedure') which establishes a three-month moratorium, thereby providing the debtor with protection from creditor enforcement action and enabling it to establish a reorganisation plan (see question 14).

Aside from the debtor, only the insolvency administrator is authorised to submit a reorganisation plan to the insolvency court. However, the creditors' meeting can instruct the insolvency administrator to prepare a reorganisation plan, which the insolvency administrator has to submit to the court within a reasonable time. The creditors' committee, if one has been appointed, the works council, the spokespersons' committee of the managerial employees, and the debtor, also have an advisory role in the preparation of the plan by the administrator.

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## Involuntary reorganisations

### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

As described above, insolvency proceedings may be commenced by a creditor on presentation of an application if it can demonstrate that the debtor is insolvent. An individual creditor does not have authority to submit a reorganisation plan. The creditors' meeting, however, may instruct the insolvency administrator to produce a reorganisation plan. If each class of creditors accepts the plan, and if the insolvency court confirms the plan, it will then come into effect.

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## Mandatory commencement of insolvency proceedings

### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Each managing director, or each member of the management board, of a legal entity (limited liability company, stock corporation, etc), a (limited liability) partnership that has solely legal entities as (general) partners, or an unincorporated company is obliged to file an application for the commencement of insolvency proceedings without undue delay and, in any event, at the latest within three weeks after the date on which the company has become illiquid or over-indebted (as defined in the Insolvency Act (see question 1)). The managing directors are not obliged to apply for the commencement of insolvency proceedings immediately if they can reasonably expect that the illiquidity or over-indebtedness will be remedied within three weeks. However, each managing director is obliged to apply for the commencement of insolvency proceedings whenever it becomes clear that this reasonable expectation will not materialise. This is mandatorily deemed to be the case after the three weeks have lapsed.

Non-compliance with the obligation to apply for insolvency proceedings as described above will expose the managing directors to a personal liability towards the company or its creditors for damages resulting from the delayed initiation of the insolvency proceedings (see question 41). Furthermore, non-compliance with such obligation is an offence under German criminal law, which is punishable with a prison term of up to three years, or a fine.

Furthermore, each managing director or each member of a management board is under a duty to immediately assess the financial situation of the company if there are indications that the company might become unable to pay its debts when they fall due or the company's total liabilities (including accruals) might exceed its total assets.

The obligation to file an application for the commencement of insolvency proceedings does not only apply to the managing directors or management board members of German entities, but also to the corresponding legal representatives of foreign companies that have their centre of main interests (COMI) in Germany.

Furthermore, each shareholder of a limited liability company is obliged to file for insolvency proceedings if:

- the company has become unable to meet its payment obligations or is over-indebted (or both); and
- the company does not have, or no longer has, a managing director.

The same applies to each member of the supervisory board of a stock corporation if the stock corporation does not have, or no longer has, a management board. Non-compliance with these obligations is an offence under German criminal law, which is punishable with a prison term of up to three years, or a fine, unless the shareholder is not aware of the company's illiquidity, over-indebtedness or that the company is without management.

In addition to personal and criminal liability, if a company carries on business while insolvent, certain transactions entered into by the insolvent company might be contested by the insolvency administrator after the commencement of the insolvency proceedings (see question 39).

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

As stated above, in insolvency proceedings the right to manage and transfer the debtor's assets passes to the insolvency administrator after the opening of the insolvency proceeding. Therefore, if the managing directors after the opening of the insolvency proceedings transfer an object forming part of the insolvency estate (without the consent of the insolvency administrator), such transfer is legally invalid (subject to certain exceptions). Once the application to open insolvency proceedings has been filed, but before an order has been made opening the insolvency proceedings, the court may appoint a preliminary administrator. Usually, a preliminary administrator has fewer powers than an administrator, although the scope is similar and, if necessary, he or she can dispose of the debtor's assets (in which case he or she is referred to as a 'strong preliminary administrator'). However, he or she is not entitled to sell the entire enterprise or one of its businesses (see question 18). The preliminary administrator's primary role is to continue the business of the debtor. The insolvency court is authorised to order that encumbered assets that are of particular significance for a restructuring must not be released to the secured creditors by the preliminary insolvency administrator. Rather, the secured creditors are only entitled to demand compensation for the loss of value caused by the preliminary insolvency administrator's usage. Liabilities incurred by a strong preliminary administrator (ie, where he or she has been authorised to dispose of the debtor's assets) are deemed to be liabilities of the estate, provided that the insolvency proceeding will actually be opened subsequently.

As far as continued trading of the debtor's business after the opening of the insolvency proceeding is concerned, creditors who supply goods or services are paid as priority creditors of the estate. Examples of priority liabilities of the estate include:

- liabilities incurred by the administrator or otherwise as a result of the administration, disposition, sale and distribution of the insolvency estate; and
- liabilities arising after the opening of the insolvency proceeding from continuing contracts (eg, employment agreements, lease agreements), and contracts which the administrator has adopted.

As referred to in question 11, section 270 of the Insolvency Act provides that the debtor may, under the supervision of an insolvency practitioner, continue to manage the insolvency estate and dispose of assets (a process called self-administration). This is not dissimilar to the debtor-in-possession provisions of Chapter 11 of the US Bankruptcy Code. The prerequisite for the proceeding is that the insolvency court orders self-administration when the debtor applies for the opening of insolvency proceedings. The conditions for the making of such an order are:

- that the debtor has applied for the order; and
- that there are no circumstances which lead to the expectation that such an order will disadvantage creditors.

Self-administration is deemed not to be to the disadvantage of the creditors, if a preliminary creditors' committee (see question 28) unanimously approves the debtor's application.

If the reorganisation plan is successful and the debtor is to continue its business once the insolvency proceeding has come to an end, the plan may provide for the continued supervision of the debtor's performance. That supervisory role is carried out by the insolvency practitioner.

Furthermore, section 270b of the Insolvency Act provides for the protective shield procedure, which puts a moratorium in place on creditor enforcement for a limited period of time. The conditions for opening the protective shield procedure are that:

- the debtor applies for it when an over-indebtedness or a threatening illiquidity (or both) has occurred (as defined in the Insolvency Act (see question 1)); and
- the intended restructuring has reasonable prospects of success.

If these requirements are met, the insolvency court may – without opening preliminary insolvency proceedings – order the moratorium on creditor enforcement for a maximum of three months during which the debtor must, under the supervision of an insolvency practitioner, establish and present a reorganisation plan. A debtor cannot apply for the protective shield procedure if it is already illiquid.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

##### Pending legal proceedings

The Civil Procedure Code imposes a stay on proceedings when the court opens insolvency proceedings. If the court has appointed a strong preliminary administrator, so that the debtor is generally prevented from selling assets during this time (see question 14), then the stay of proceedings commences when the court appoints the preliminary administrator.

Once insolvency proceedings have been formally opened, the administrator is entitled to choose whether to continue with legal proceedings initiated by the debtor pre-insolvency.

##### Enforcement of claims

Once insolvency proceedings have been formally opened creditors are prevented from enforcing their claims. In certain circumstances, the court could impose a stay on the initiation of enforcement of claims or suspend pending enforcement action prior to the formal opening of insolvency proceedings. Note that, as regards pending enforcement action over immovables, only the court seized with the claim has the right to suspend such action.

Creditors cannot, in general, apply to the court to lift this moratorium on enforcement action. There are, however, exceptions. Creditors who can show that an asset does not belong to the estate because of a right of segregation may enforce their claim irrespective of the insolvency proceedings. Creditors with a right to separate satisfaction are also exempted; they may claim preferential satisfaction of their claim from the respective asset.

In respect of financial institutions that are subject to the Banking Act, the FSA may temporarily suspend transactions by and against the institution to avoid its insolvency, for example, by ordering a moratorium.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Generally, the insolvency administrator may enter into loans and other credit to secure the necessary financing for a continuation of the debtor's business. Such liabilities incurred by the administrator are treated as priority liabilities of the insolvency estate. As priority liabilities, they will be settled prior to the satisfaction of unsecured creditors, albeit only after the costs of the insolvency proceedings, which are also priority liabilities, and the secured creditors have been satisfied. If a debt is to be incurred that would significantly burden the insolvency estate, the insolvency administrator must obtain the consent of the creditors' committee or, if a creditors' committee has not been appointed, the consent of the creditors' meeting.

To enable a successful restructuring, a reorganisation plan can also give priority to creditors that either:

- make loans or give credit to the debtor or a takeover company during the period of supervision (which follows the ratification of the plan); or

- permit existing loans or credits to continue during this time.

Those liabilities are also priority liabilities. They will not only be paid prior to satisfaction of unsecured creditors already existing, but also to new creditors entering into contractual agreements with the debtor within the period of supervision, while secured creditors will still be paid first. The aggregate maximum amount of such priority credit will be fixed in the plan. Further, such preferential satisfaction requires an agreement between the debtor or takeover company and the respective creditor and written approval by the insolvency administrator.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

As a general principle, claims by or against the insolvency estate existing as at the date of the opening of the insolvency proceedings may be set off against each other:

- if the claim of the creditor existed and was due and payable at the time of the opening of insolvency proceedings; and
- if the claim of the estate against which the creditor wishes to effect set-off was also existing at the time of the commencement of insolvency proceedings.

In the event that the claim or cross claim is contingent or not yet due at the date of the opening of insolvency proceedings, the set-off may only be effected once the claim becomes unconditional or due. A set-off will be excluded if the claim of the estate that is to be offset becomes unconditional or due prior to the time that the set-off can be effected by the creditor.

No set-off is permissible if:

- a creditor's claim arises after the opening of the insolvency proceedings;
- a creditor's acquires its claim from another creditor following the opening of the insolvency proceedings (even if the original creditor's claim pre-dated the insolvency);
- a creditor's acquires the right to set off by means of a voidable transaction; or
- a creditor is a debtor of the insolvency estate and has a claim which has to be satisfied from the assets of the debtor which are not affected by insolvency (eg, because of a contract entered into with the debtor who has upon the opening of insolvency proceedings no power to dispose of its assets).

These restrictions on a set-off may not affect:

- the transfer of financial collateral arrangements (as defined in section 1(17) of the Banking Act, for example, cash deposits, pledges or fiduciary transfers of securities); or
- the netting of claims under securities settlement systems (as defined in section 1(16) of the Banking Act) if the netting takes place on the day of the opening of the insolvency proceedings, at the latest.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

Upon the opening of insolvency proceedings, which include either a reorganisation or liquidation, the insolvency administrator is entitled to sell the debtor's assets of the debtor. If the insolvency administrator intends to effect transactions of special significance to the insolvency proceedings, he requires the approval of the creditors' meeting or the creditors' assembly. In particular, such approval is necessary if the entire enterprise, or one of its businesses, is to be transferred.

In practice, most administrators aim to sell the business as a going concern by way of an asset sale as soon as possible to realise the best

possible price and to preserve the greatest possible number of jobs. In general, the sale of assets is free and clear of any liability on the part of the buyer, provided that the insolvency proceedings have actually been opened. However, such asset sale does not generally affect creditors with security rights in rem to the assets. As a rule, the insolvency administrator is entitled to dispose of encumbered moveable assets that are in the possession of the debtor and subsequently pay off the secured creditors with the proceeds from the sale. In practice, the insolvency administrator usually provides to the acquirer of the debtor's business (or certain parts thereof) with a release letter from the main secured creditors confirming that the security will be released upon payment of the purchase price. Apart from this, under section 613a of the Civil Code, the sale of a business (as a whole or in part) causes all employment relationships pertaining to this business (or the respective part sold) to be transferred by operation of law to the buyer (unless the employees concerned object to the transfer of their employment).

Subject to creditors' meeting approval, the insolvency administrator is free to pursue 'stalking horse' bids in a sale procedure. In practice, however, such bids do not seem to be of major relevance as the insolvency administrator will usually aim at disposing of the debtor's business as soon as possible, so will not focus too much on preliminary 'stalking horse' bids that could considerably delay the sales procedure (and finally jeopardise the sale of the business as such). If the administrator expects that a number of parties might be interested in acquiring the debtor's business, he or she will initiate an auction process to obtain the best possible price (and preserve the likelihood of a sale in a well-ordered process).

Under the Insolvency Act, a creditor may not credit bid in the sales process (unlike in a security enforcement process initiated by creditors outside of insolvency proceedings). It is possible, however, for the administrator and the acquirer of the debtor's business, who is also creditor, to agree that the consideration owed by the acquirer is (partly) paid by way of a set-off or waiver (subject to creditors' meeting approval). If the acquirer's claims against the debtor are only unsecured insolvency claims (which will be the normal case), these claims will not be considered at nominal value, but will likely be valued at a percentage equalling the expected insolvency quota. As to assigning a claim of a (secured) creditor, there are no restrictions under the Insolvency Act. If a creditor aims to acquire the business of the debtor (ie, the insolvent company), it is, however, more likely that this will be achieved by a debt-to-equity-swap as part of an insolvency plan (see question 23).

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

There are no specific statutory provisions dealing with intellectual property rights in insolvency. In the event of the insolvency of the licensee, the insolvency administrator has the right to continue the licence agreement under its present terms or reject its continuation (any claims for damages of the licensor for non-performance being insolvency claims see question 21). Contractual clauses providing for a right of the licensor to terminate the licence agreement upon the opening of insolvency proceedings over the estate of the licensee will, at least according to the prevailing view, be void.

In the event of the insolvency of the licensor, the different types of licences (exclusive and non-exclusive, main licences and sublicences) and intellectual property rights (patents, trademarks, copyrights, etc) need to be reviewed individually to determine whether the licensee is still the owner of a licence and authorised to use it. Generally, the administrator over the estate of the licensor has a right to opt to continue the licence agreement. In respect of an exclusive copyright main licence (for software, films, etc), the High Court of Mannheim held that the choice of non-performance resulted in the licensee's loss of the licence (judgment of 27 June 2003, 7 O 127/03).

A judgment of the Federal Supreme Court (17 November 2005, IX ZR 162/04) shows a possible way to ensure the continuous use of software by the licensee in the event of a licensor's insolvency. In that case, the licence agreement allowed both parties to terminate the

agreement if the continuation of the agreement was unacceptable to one party. The agreement further provided for a transfer of the source code of the software developed by the licensor to the licensee under the condition precedent of such termination, the licensee in this event being obliged to pay a one-off compensation to the licensor. In the insolvency proceedings over the estate of the licensor, the insolvency administrator chose not to continue the licence agreement. Therefore, the licensee terminated the agreement. The court held that:

- the insolvency administrator had the right to choose not to further perform the licence agreement;
- because of this, the licensee had the right to terminate the agreement; and
- as the transfer of the source code was already effected before the commencement of insolvency proceedings (though under a condition precedent that was only fulfilled after the commencement of the insolvency proceedings), this transfer was not affected by the commencement of the insolvency proceedings and subsequent actions of the insolvency administrator.

In a recent judgment (21 October 2015, I ZR 173/14), the Federal Supreme Court also stated that, under certain circumstances, insolvency administrators shall no longer be entitled to reject or assume contracts in relation to licence buy-outs once the mutual obligations of the parties to the licence agreement have been fulfilled.

Furthermore, the *M2Trade* (I ZR 70/10 of 19 July 2012) and *Take Five* (I ZR 24/11 of 19 July 2012) judgments of the Federal Supreme Court stated that even if an (insolvent) sub-licensor loses the main licence in an insolvency proceeding over its estate, any sub-licensee will still retain its sublicense (ie, the loss of the main licence does not automatically end the sublicense). In these judgments, the Federal Supreme Court also indicated a tendency to treat all intellectual property right sublicences in the same way. Whether this will also apply to main licences remains unclear.

#### Personal data in insolvencies

##### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

In addition to the Federal Data Protection Act, the Insolvency Act does not provide for any specific restrictions on using customer data within an insolvency proceeding. Therefore, it is not uncommon that, in particular, the customer base of an insolvent company, which often represents an asset of significant value, is sold as part of an asset deal between the insolvency administrator and a third party (see question 18 regarding asset deals). In this context, it should, however, be noted that in a recent case, the Bavarian Data Protection Authority (DPA) imposed a significant fine (a five-figure amount) on both the seller (ie, the appointed insolvency administrator) and the purchaser in connection with the sale of customer personal data. According to the DPA, customer personal data (eg, customer email addresses, phone numbers, credit card information, etc) as part of an asset deal had been transferred unlawfully (in violation of the Federal Data Protection Act), since the insolvency administrator and the purchaser failed to obtain customer consent or, alternatively, give the customers an opportunity to object to the transfer of the personal data.

#### Rejection and disclaimer of contracts in reorganisations

##### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

Generally, any mutual contracts not having been performed by either party in full at the time of the formal opening of the insolvency proceedings become unenforceable, unless the insolvency administrator chooses to adopt the contract. The counterparty to such contract can require the insolvency administrator to decide without delay whether he adopts the contract. If he does not do so after having received such request, his option to elect a performance of the contract falls away.

Any damages incurred by the other party as a result of such avoidance of contract may be filed as an ordinary, unsecured insolvency claim.

Contracts for the sale of goods by the insolvent company that are subject to retention of title remain in place upon request of the purchaser if possession of the goods was transferred to the purchaser prior to the formal commencement of the insolvency proceeding. If, on the other hand, the insolvent company prior to the opening of the proceedings has purchased goods and received possession of such goods subject to retention of title by the seller, the insolvency administrator may postpone his or her decision on the option to maintain the contract until the date of the information hearing (see question 26).

As regards contracts for the lease of real estate if the insolvent company is the tenant, the insolvency administrator may terminate the lease giving the relevant statutory notice period (irrespective of the agreed contractual term). The landlord is not entitled to terminate a contract because of insolvency of the tenant.

Employment contracts where the insolvent company is the employer may be terminated by either party with a notice period of three months irrespective of any contractual provision to the contrary. In the insolvency proceedings, employees can be made redundant with the benefit that severance payments under a social plan are capped at an aggregate maximum amount of two-and-a-half times the monthly salary per employee. However, even after the commencement of the insolvency proceedings, the Employment Protection Act still applies, which may constrain redundancies by the insolvency administrator.

In self-administrations (section 270 et seq of the Insolvency Act (see questions 11 and 14)), the provisions on the performance of mutual contracts in an insolvency scenario also apply allowing the self-administering management of the insolvent company to exercise the insolvency administrator's rights. The self-administering management is, however, supervised by an insolvency practitioner whose consent is required for certain measures.

Where an insolvency administrator (or in the event of a self-administration the debtor) breaches the aforementioned mutual contract, the other party can claim the resulting damage. Such damage claim would be an estate claim taking priority over insolvency claims (see question 31). However, if the insolvency administrator (or in the event of a self-administration the debtor) has opted for the non-performance of the contract the resulting damage may only be filed as non-preferred insolvency claim (see above).

#### Arbitration processes in insolvency cases

##### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

There are no statistics addressing the number of arbitration proceedings in conjunction with insolvency proceedings.

After the opening of insolvency proceedings, the debtor loses its ability to be a party to a dispute in relation to the estate; instead, the insolvency administrator will be the right party. In principle, the insolvency administrator is – subject to certain exceptions – bound by an arbitration clause agreed by the debtor pre-insolvency. However, an arbitration clause agreed by the debtor prior to the opening of insolvency proceedings does not affect indispensable rights of the insolvency administrator, so that the insolvency administrator is not bound by an arbitration clause in respect of, for instance, avoidance claims pursued by the insolvency administrator or proceedings related to the insolvency administrator's right to reject the fulfilment of a contract. Also, the insolvency administrator may refuse to submit to arbitration proceedings if there is insufficient money in the estate to cover the expenses of such proceedings. The insolvency court does not have the authority to direct the insolvency administrator to submit a dispute to arbitration. The insolvency administrator is, however, bound by an arbitration (clause) he or she has agreed with the other party involved.

Apart from the aforementioned exclusions in relation to the insolvency administrator's intrinsic rights there are no types of insolvency disputes that may not be arbitrated. Where insolvency administrator is willing to enter into an arbitration agreement in an insolvency proceeding, the consent of the creditors' committee has to be obtained.

Where the insolvency administrator rejects the claim or another creditor objects to its insertion in the insolvency table then a creditor may need to bring proceedings to have the claim recognised. This may involve having to litigate or arbitrate an underlying dispute. In such litigation or arbitration the court or tribunal will be asked to make a declaration (rather than order specific performance). If the arbitration tribunal grants a declaration that the underlying claim is valid the creditor would be permitted to be included in the insolvency table. Where the counterparty obtained an arbitral award prior to the opening of insolvency he can file such claim with the insolvency table (although the insolvency officeholder could appeal the award).

The opening of insolvency proceedings does not automatically cause arbitration proceedings to be interrupted. Whether arbitration proceedings are interrupted or not depends mainly on the procedural rules applied by the arbitral tribunal. In any case, the insolvency administrator must have the chance to be heard in the arbitration proceedings. Otherwise, the arbitration award will not be recognised by German (insolvency) courts.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

The Insolvency Act places very few restrictions on what may be included in a reorganisation plan (such plan is called an 'insolvency plan' in Germany). By approving a plan, the parties can, inter alia, agree to deviate from the statutory rules on the disposition of the debtor's assets and the distribution of proceeds. The plan must describe the proposed measures for reorganising the debtor and how the plan affects the rights of creditors. Typically, a plan will contain provisions for a partial waiver of claims or for deferred payments. It will also usually set out the likely outcomes for creditors in a liquidation and a reorganisation of the business, so that the creditors can evaluate for themselves the (financial) advantages of a reorganisation.

The insolvency plan must separate creditors into classes. In particular, it must distinguish between secured and unsecured creditors. The plan must be approved by each class of creditor. A class of creditors accepts the plan if a majority in number and majority in value in that class vote in favour. It is then up to the court to decide whether to confirm the plan.

Furthermore, creditors who have not filed their claims with the insolvency practitioner and had them included on the official table are also bound by the measures approved through the insolvency plan. Such creditors will be treated as creditors of the appropriate class if they assert a claim against the debtor after the insolvency proceedings have been terminated (see also question 23).

As the insolvency plan can provide for the disposition of the debtor's assets, it may create releases by the debtor in favour of third parties (eg, releasing the management, advisers or lenders of the debtor company from a potential liability). Such releases become effective upon the creditors' consent to and the insolvency court's approval of the insolvency plan.

Furthermore, an insolvency plan may provide for all types of (restructuring) measures permissible under corporate law, especially a debt-to-equity swap. Where a debt-for-equity swap is planned, the shareholders need to vote on the insolvency plan in addition to the creditors. Shareholders will form a separate voting class. A class of shareholders accepts the plan if a majority in value in that class votes in favour of the plan. As under the German corporate law, this majority is sufficient here even without a majority in number.

As regards a debt-to-equity swap, each creditor who is to acquire an equity participation must consent. It is not sufficient that the class has been consulted, ie, it is not possible to force a lender to convert a loan into equity.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

As stated above, the debtor is entitled to file an application for the opening of insolvency proceedings when illiquidity is threatened. At the same time, the debtor can apply for self-administration, which would allow the debtor to continue manage the insolvency estate under

supervision, and submit an insolvency plan for a reorganisation of the business (a 'pre-packaged' plan (see question 24)). In practice, a pre-packaged plan will often be discussed with the debtor's main creditors before it is filed to ensure that they will not oppose it once insolvency proceedings have been initiated.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A proposed insolvency plan must first be considered by the insolvency court. The insolvency court will reject the plan if:

- the formalities with regard to the authority to submit the plan and with regard to its contents – especially regarding class constitution – have not been observed;
- a plan submitted by the debtor clearly has no chance of being accepted by the creditors or confirmed by the court; or
- the claims to which the participants are entitled by the plan can obviously not be satisfied.

If the plan is not rejected on any of these grounds, the insolvency court will set a date for a hearing at which the insolvency plan and the creditors' voting rights can be discussed and the plan will be voted on (the 'hearing for discussion and voting'). Each class of creditors will vote separately on the plan. A plan will be accepted if each class of creditors accepts the plan by a majority in number and value. A class of shareholders accepts the plan if a majority in value in that class votes in favour.

Even if the required majority is not attained, the consent of a voting group is deemed to be given, if:

- the members of that group are not disadvantaged to a greater extent than they would be on the liquidation of the debtor's business and a disposal of its assets by the administrator;
- the members of that group have a reasonable share of the economic value that was to accrue to the participants in the plan; and
- the majority of the other voting groups have consented to the plan.

Following the acceptance of the plan by the creditors and shareholders the plan must be ratified by the insolvency court. The insolvency court will not ratify the plan if, inter alia, acceptance of the plan by the creditors (and shareholders) was obtained in a wrongful manner, including as a result of, but not limited to, preferential treatment of a creditor.

Furthermore, the court may refuse to ratify the plan if a creditor (or shareholder) successfully objects to and/or appeals the plan (see question 30).

Generally, a default by the debtor in performing an approved plan does not affect the validity of the plan. However, in the event that claims of creditors are deferred or partially waived as part of the plan, that deferment or waiver ceases to bind that creditor if the debtor falls into significant arrears in the performance of the plan. The debtor will be deemed to have fallen into 'significant arrears' if it fails to pay a due liability despite the creditor making a written demand and setting a minimum period of two weeks for payment.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

In principle, all decisions of the insolvency court require notice to all the persons affected. Notwithstanding this, public notifications are sufficient for proof of service on all parties, even where the Insolvency Act provides for personal service. Thus, creditors should pay attention to all public notifications issued by the insolvency court and keep in contact with it.

The creditors have a right to be informed by the insolvency administrator about the affairs of the insolvency estate. The insolvency administrator will usually fulfil his or her duty to provide information at creditor meetings (in particular the information hearing, see below)

by giving a detailed report on the financial situation of the debtor, the reasons for the insolvency, the prospects of a successful restructuring, the feasibility of an insolvency plan, the impacts on the satisfaction of creditors and on measures already taken by the administrator prior to the meeting.

With regard to meetings, a creditors' meeting can only be called by the insolvency court. The most important creditors' meetings are:

- information hearing – at this first meeting, the creditors mainly resolve, based upon a report by the administrator, whether to continue or partially or completely shut down the debtor's business. The creditors also resolve whether creditors' committee should be established, the approval of which would be required before certain measures can be taken by the administrator, for example, significant transactions;
- examination hearing – at this meeting, the registered claims are examined;
- hearing for discussion and voting – at this meeting, an insolvency plan and the creditors' voting rights are discussed and the plan is voted on; and
- final hearing – the purpose of this meeting is for a discussion of the administrator's final statement of fees, the raising of any objections against the final list of creditors and a decision by the creditors as to the assets of the insolvency estate that cannot be realised. The insolvency court also decides on the final distribution.

When the insolvency court makes the order opening the insolvency proceeding, it also sets dates for the information hearing and the examination hearing, which can take place on the same day.

Under the German Insolvency Act, an insolvency plan cannot create a release of liabilities owed by third parties to the creditors as insolvency plans may only govern (restructuring) measures in relation to creditors and shareholders of the insolvent entity.

Moreover, it is explicitly regulated that an insolvency plan may not affect the rights entitling creditors of insolvency proceedings against a debtor's co-obligors and guarantors (section 254(2) of the German Insolvency Act). In practice, this often complicates the restructuring of a corporate group if the parent company is insolvent and its subsidiaries are co-obligors or collateral providers, or both.

However, an insolvency plan may create releases by the debtor in favour of third parties (eg, releasing the management, advisers or lenders of the debtor company from a potential liability) (see question 23).

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Once insolvency proceedings have been opened, only the insolvency administrator may pursue claims belonging to the estate. The insolvency administrator cannot authorise a creditor to pursue a claim. In certain cases, the insolvency administrator may authorise the debtor or, respectively, its representatives to pursue a claim in court; however, this would not be a solution if the estate is insufficient to pursue the claim. Legal aid is available to an insolvency administrator, provided that:

- the costs of the lawsuit are not covered by the estate;
- the advancement of the costs by those who have an economic interest in the success of the lawsuit is unacceptable to them;
- the lawsuit has adequate chances of success; and
- the pursuit of the claim is not arbitrary.

Thus, no legal aid will be granted if (certain) creditors are able to advance the costs and if such creditors benefit from the lawsuit, because of a substantial increase of their quota. In many cases, the granting of legal aid for a lawsuit of the insolvency estate is denied, because there are creditors who would benefit from the lawsuit and who could advance the costs of the lawsuit, but are unwilling to do so. In any case, the insolvency administrator is free to enter into a loan to finance the costs of the lawsuit. The repayment obligation of the loan would be an estate claim taking priority over ordinary unsecured insolvency claims (see question 33).

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The insolvency court is generally obliged to appoint a preliminary creditors' committee in conjunction with the opening of preliminary insolvency proceedings, if the debtor meets two of the three following thresholds:

- balance sheet total of at least €6 million;
- annual turnover of at least €12 million; and
- at least 50 full-time employees.

In all other cases, the insolvency court may appoint a preliminary creditors' committee upon request of the debtor, the preliminary insolvency administrator or a creditor. The preliminary creditors' committee can require the insolvency court to appoint a certain independent person as preliminary insolvency administrator and has the right to suspend an early self-administration procedure (see question 14).

In the first creditors' meeting, the creditors will have to decide whether the preliminary creditors' committee is to be maintained and, if so, whether certain members of the committee should be removed and whether additional members should be appointed. In the preliminary creditors' committee and in the final creditors' committee, creditors with a right to separate satisfaction (see question 26), the largest insolvency claim holders, the minority creditors and the employees are to be represented. However, there are no rules on the composition of the final creditor's committee. The members of the creditors' committee are responsible for supporting and monitoring the insolvency administrator. For this purpose, the members of the creditors' committee have numerous powers and responsibilities. They must, primarily, keep themselves informed about the business of the debtor, examine the debtor's books and implement a cash audit. If the insolvency administrator intends to effect transactions of special significance, he needs the approval of the creditors' committee. In particular, such approval will be necessary if the entire enterprise, or one of its businesses, is to be transferred.

The members of the creditors' committee are entitled to adequate compensation for their function as members of the creditors' committee and to reimbursement of necessary expenses. Expenses incurred through retaining advisers will only be reimbursable if these are proportionate and necessary to properly fulfil the duties as a member of the creditors' committee.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

There are no provisions on group insolvencies (yet). German insolvency law strictly adheres to the principle 'one debtor, one estate, one procedure'. Therefore, a combination of the assets and liabilities of group companies into one pool (substantive consolidation) is not permitted. Also, a combination of the procedures (joint administration or procedural consolidation) is not possible under German insolvency law. However, provided that the same insolvency court and the same judge has jurisdiction to open the proceedings with respect to several group companies, there is a possibility to have the same insolvency administrator appointed for all proceedings, thereby assuring a factual coordination. The competent judge has discretion to appoint the same insolvency administrator for the insolvency proceedings of several group companies to optimise the coordination, or to refuse such (joint) appointments to avoid possible conflicts of interest.

Assets belonging to the insolvency estate of the German debtor may only be transferred to an insolvency estate of a debtor in another country based on either:

- a supply and delivery agreement between the two debtors that has not been terminated following the insolvency; or

- an asset sale and purchase agreement entered into by the insolvency administrators (ie, on the basis of continuing or new contractual arrangements).

It should be noted that, on 30 January 2014, the German government passed an official legislative draft bill that aims to facilitate the handling of group insolvencies ('Act on the Facilitation of the Handling of Corporate Group Insolvencies'). In essence, the draft bill intends to address the challenges of group insolvencies by introducing the following provisions:

- an optional common place of jurisdiction for the different insolvency proceedings;
- the obligation on the different insolvency courts to coordinate with each other on the appointment of one joint insolvency administrator for the group-wide insolvency proceedings;
- an obligation of the different insolvency courts, insolvency administrators and creditors' committees to cooperate; and
- coordination proceedings to further enhance the coordination between the different insolvency proceedings over group entities.

As far as cross-border insolvencies of corporate groups within the EU are concerned, please see questions 47 to 49 for more details.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Orders or decisions of the insolvency court can only be appealed where the Insolvency Act expressly provides for an immediate appeal (ie, there is no automatic right of appeal). Notwithstanding this, a simple appeal is possible if the decision in question is not made by the judge, but by the clerk of the court. In any case, a creditor will only be entitled to appeal if its claim is rejected or its rights are violated by the decision.

The provisions for an immediate appeal are set out in sections 6 and 4 of the Insolvency Act in connection with section 567 et seq of the Civil Procedure Code.

The time limit for filing an immediate appeal is two weeks beginning upon the pronouncement or upon the service of the judgment to be challenged. The appeal must be filed by a written notice to the insolvency court that has to decide whether it wants to grant intermediate relief.

Pursuant to section 574 et seq of the Civil Procedure Code, an appeal on points of law can be used to challenge decisions resulting from an immediate appeal. However, such appeal is only admissible if the appeal court has permitted to do so in its order following the immediate appeal. Such permission to file a complaint on points of law shall be granted by the appeal court if:

- the legal matter is fundamentally important; or
- a judgment is required for the purposes of advancing the law or for ensuring consistency of court decisions.

Neither the Insolvency Act nor the Civil Procedure Code provides for requirements to post security to proceed with an appeal.

As far as reorganisation through insolvency plans is concerned, on the application of any creditor (or shareholder), the court may refuse to ratify an insolvency plan if:

- the applicant objects to the insolvency plan by no later than the hearing for discussion and voting; and
- can demonstrate that he or she will be put in a less favourable position than he or she would have been in the absence of the insolvency plan.

Irrespective of such an application, the court shall ratify the plan if the insolvency plan provides for funds being made available for compensation in the event that a concerned party shows to the satisfaction of the court that it will be placed in a less favourable position, which is to be determined in a separate proceeding.

Furthermore, at the request of the insolvency administrator, the insolvency court may dismiss an appeal against the court order by which an insolvency plan is confirmed without delay, if it appears that the immediate effectiveness of the insolvency plan should take

precedence, because the harm that would ensue on delaying implementation of the insolvency plan outweighs the losses sustained by the applicant. In such a case, the appellant will be compensated out of the insolvency estate for the losses sustained by implementation of the insolvency plan.

### Claims

#### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

The order opening the insolvency proceeding, when sent to creditors or publicised, will include a notice to creditors requiring them to submit their claims to the administrator within a period of between two weeks and three months from the date of the order. It will also include a request to creditors to notify the administrator promptly if they claim to have security over the debtor's chattels or immovable assets. The subject, nature and basis of the security right and the claim secured should also be stated.

Creditors are obliged to register their claims with the administrator in writing, stating the basis and the amount of the claim. Copies of documents supporting or evidencing the claim must be attached to the written statement by which the claim is asserted. If the amount of the claim cannot be determined exactly at the time the claim is registered, the claim has to be registered based on a fair estimate of the value as at the date of the opening of the insolvency proceeding. Claims that are subject to a condition precedent can be registered with the administrator and must be considered when proceeds are distributed. Respective amounts are, however, not distributed, but retained by the administrator either until the condition precedent is fulfilled, in which case the amount is released to the relevant insolvency creditor, or until it becomes clear that the condition precedent will not be fulfilled, in which case the proceeds are free for distribution to the other insolvency creditors. At the examination hearing, the registered claims will be examined to determine amount and ranking. In principle, claims that are registered after the expiry of the registration period can still be examined. A claim is deemed to have been admitted where no objection has been raised by either the administrator or another creditor.

The insolvency court will then prepare a table of registered claims showing which claims have been admitted and setting out the amount and the ranking of each claim. Inclusion in the table has the effect of a final judgment as far as the administrator and the creditors are concerned. Creditors who have claims which have not been objected to by the debtor may enforce such claims after termination of the insolvency proceedings by way of execution as they can under any normal executable judgment. Thus, an objection by the debtor cannot hinder the admission of a claim but may prevent the creditor from executing his claim on the basis of the entry in the table.

If a creditor's claim is disputed by the administrator or another creditor, the creditor can bring proceedings before an ordinary court for a decision as to whether its claim should be admitted.

Generally, all claims rank equally, preferential and subordinated claims being the exception. Among the subordinated claims, shareholder loans are of particular importance. All shareholder loans made by lenders holding more than 10 per cent of the shares in the borrower (ie, a company or a partnership that has no individual persons as general partners) are generally classified as subordinated insolvency claims. Furthermore, a repayment of such shareholder loan made in the year prior to the opening of insolvency proceedings will generally be voidable. Prior to an insolvency, shareholder loans may, however, be repaid, provided that such repayment is not restricted by a subordination agreement.

It should be noted that the provisions on shareholder loans should generally apply to all insolvency proceedings commencing on or after 1 November 2008. Prior to that date the far more complex rules on equity substituting shareholder loans were in force. Those were fully replaced on 1 November 2008, but in certain scenarios they are still applicable. In simple terms, the rules on equity substituting shareholder loans should still apply to insolvency proceedings commenced before 1 November 2008. Furthermore, any claims having come into

existence prior to 1 November 2008 under the former provisions on equity substituting shareholder loans may have 'survived' the change of law, and may, therefore, still be relevant.

There are no specific provisions that deal with the purchase, sale or transfer of claims against the debtor and there is no general obligation to disclose such transfer of claims. However, setting off claims against the insolvency estate is not permitted if a creditor acquires his claim from another creditor after the opening of the insolvency proceedings (notwithstanding that the acquired claim may have originated prior to the opening of insolvency proceedings).

Creditors who acquire a claim at a discount are entitled to claim for its full face value (ie, they may file the full amount with the insolvency administrator).

Generally, creditors can claim interest that has accrued after the opening of insolvency proceedings. However, interest accruing on such claims from the opening of the insolvency proceedings is subordinated to other claims of insolvency creditors. They will only be paid when all other creditors' claims have been satisfied. However, they rank higher than further subordinated claims such as the costs incurred by the insolvency creditors because of their participation in the proceedings; fines, regulatory fines, coercive fines and administrative fines; claims to the debtor's gratuitous performance of a consideration; and shareholder loans (subject to certain exceptions – see question 31).

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### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

Under German insolvency law, the insolvency court has no competence to modify the priority of a creditor's claim.

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### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Under the Insolvency Act, in general, there are no priority claims. In particular, employee-related claims relating to a period prior to the opening of insolvency proceedings do generally not enjoy priority status.

However, employees are protected by 'insolvency money', which covers wages for a period of up to three months prior to the opening of the insolvency proceedings.

The opening of insolvency proceedings does not affect creditors with proprietary claims for the return of assets that do not belong to the insolvency estate. Secured creditors may also enjoy certain superior rights. Furthermore, claims and costs arising from transactions executed by the administrator after the opening of the insolvency proceedings attract priority status, ie, they need to be paid prior to the satisfaction of unsecured creditors, albeit after creditors with a right to separate satisfaction or a right to set off (see also question 16).

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Generally, the opening of insolvency proceedings over the estate of the employer does not affect the relationship with the employees. Claims of the employees against their employer that came into existence prior to the opening of insolvency proceedings are in general considered as ordinary insolvency claims with no priority; claims of the employees against their insolvent employers that come into existence after the opening of insolvency proceedings attract priority status as estate debts.

Employment contracts where the insolvent company is the employer may be terminated by either party with a notice period of three months, (irrespective of any contractual provision to the contrary or an exclusion of termination). However, even after the opening of the insolvency proceedings, the Employment Protection Act still applies, which may constrain redundancies by the insolvency administrator. The German Insolvency Act contains, a number of provisions which facilitate and accelerate consultation processes with the works council

on operational changes that lead to redundancies and help to procure an effective termination of employment relationships, for example, protection from dismissal is limited in the event a list of employees to be made redundant has been agreed with the competent works council in a balance of interests or been approved by the labour law court in advance of issuing the notice letters. Where no works council exists, the redundancies will not trigger any severance payments under social plans. In the event that a works council had been established before a redundancy decision was taken, redundancies can be made during insolvency proceedings with the benefit that severance payments under a social plan are in any event capped at an aggregate maximum amount of two-and-a-half times the monthly salary per employee. For pension claims, see question 35.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Employees' pension claims do not enjoy priority in insolvency proceedings unless they were secured by a specific collateral in the individual case and are thus treated preferentially compared to any other regular claim. However, pension commitments of the (insolvent) employer in relation to the employees are in general protected by the German pension insurance association. In simple terms, the German pension insurance association assumes the obligation of the insolvent employer to satisfy vested pension claims and, in turn subrogated in the insolvency as a non-prioritised creditor.

Claims for deficiencies in an external pension plan or a pension scheme do not enjoy priority in the insolvency of an employer. Where pensions are granted through a pension fund, however, the insolvency protection via the German pension insurance association is also available to the employees in the event that the assets of the external pension fund do not suffice.

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Generally, the insolvency administrator (or in the event of self-administration the debtor's management board) is responsible for fulfilling the debtor's public law obligations in the insolvency proceedings (eg, obligations resulting from environmental problems). Claims and costs arising from fulfilling such obligations attract priority status (see question 33).

However, the insolvency administrator is entitled to release objects from which public law obligations derive (eg, land) from the insolvency estate so that they become part of the debtor's assets not affected by the insolvency. In this case, the government would engage a third party to solve the environmental problems. According to case law of the Federal Administrative Court, the resulting claims of the government are either be treated as priority claims (see question 33) or as unsecured insolvency claims. This depends on the grounds of the liability:

- if there is a liability for the status of the object (eg, the owner exercises legal or actual control over the polluted site that contravenes the regulations), the government would have a priority claim;
- if there is a liability for the behaviour of the debtor as polluter prior to the opening of the insolvency proceedings (eg, a debtor causes the pollution of the site through his or her actions), the government would not have a priority claim, but an unsecured claim; and
- if there is a liability of an operator of a plant, the government would have a priority claim.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Provided that the debtor is reorganised by way of an insolvency plan, debts of the debtor only survive the cessation of the insolvency proceedings if and to the extent they are specified in the insolvency plan.

This also applies for creditors who have not filed their claims with the insolvency practitioner and had them included on the official table. Such creditors are bound by the measures approved through the insolvency plan and will be treated as creditors of the appropriate class of creditors if they assert a claim against the debtor after the insolvency proceedings have been terminated. If, following the termination of the insolvency proceedings, any enforcement by these creditors jeopardises the enforcement of the insolvency plan, the insolvency court may, upon a request by the debtor, entirely or in part unwind an enforcement or deny it for a maximum of three years. Moreover, any such claims made by these creditors shall become statute-barred after one year.

A third party that acquires the debtor's business by way of an asset deal is generally not liable for any debts of the debtor, provided that the insolvency proceedings have actually been opened. The acquirer may, however, be held liable for the clean-up costs of polluted land acquired from the insolvency estate.

On the acquisition of the debtor's business (as a whole or in part) by way of an asset deal, the employees working in the business (or the respective part thereof) transfer to the purchaser by operation of law, unless the employees concerned object to the transfer of their employment relationships (see section 613a of the Civil Code). A dismissal of employees for the sole reason of the transfer is not permitted, even if the acquisition of the business is made out of an insolvency estate. However, redundancies may still be made for operational reasons, for example, to make the reorganisation of the business possible (see sections 125 to 128 of the Insolvency Act). Furthermore, the transfer of the employment relationships by operation of law does not encompass the employees' claims and pension rights arising prior to the opening of the insolvency proceedings.

Subsequent to the termination of the – regular – insolvency proceedings (ie, without an insolvency plan), creditors may – in principle – assert their remaining claims against the debtor without any insolvency related restrictions. In this context, it should be noted however, that, once the insolvency proceedings have been completed, any legal entity or partnership will, in general, cease to exist and be removed from the commercial register.

## Distributions

### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Distributions may be made whenever there is sufficient cash in the insolvency estate. However, the administrator has to obtain the consent of the creditors' committee, if one has been appointed, before each distribution. The final distribution takes place once all the assets of the estate have been realised, but only after the consent of the insolvency court has been obtained.

Distributions pursuant to an insolvency plan are not restricted by the terms of the Insolvency Act and, therefore, payments to creditors should be consistent with what has been agreed by the creditors in the plan.

## Transactions that may be annulled

### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The avoidance provisions are set out in sections 129 to 146 of the Insolvency Act.

Once insolvency proceedings have been opened that include either a liquidation or reorganisation, the administrator may set aside transactions which prefer one creditor over another or where there has been a fraudulent conveyance. In order to exercise the avoidance right, an informal declaration by the insolvency administrator is sufficient. Furthermore, the insolvency administrator is entitled to close a dispute by way of an out-of-court settlement. If the creditor rejects the avoidance, the insolvency administrator has to sue the creditor before the civil courts. An insider has the burden of proving that the transfer was not preferential or fraudulent. In general, an insider has a close relationship to debtor. If the debtor is a legal person or a company without legal personality, insiders are, *inter alia*, the members of the body representing or supervising the debtor, as well as his general partners and persons holding more than one quarter of the debtor's capital, and a person or a company that has on the basis of a comparable association

with the debtor under company law or under a service contract the opportunity to become aware of the debtor's financial circumstances. Anything that was transferred, disposed of or yielded from the assets of the debtor by means of a voidable transaction has to be restored to the insolvency estate.

Furthermore, the administrator can challenge the repayment of shareholders' loans if the repayment was made within the previous year prior to the filing for the opening of insolvency proceedings (see question 31).

In addition, any security over the debtor's assets obtained by execution of a judgment in the month prior to the application to the insolvency proceedings, or subsequent to such application, will be set aside by operation of law as at the date of the opening of the insolvency proceedings.

## Proceedings to annul transactions

### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

Once insolvency proceedings have been commenced that include either a reorganisation or liquidation, only the insolvency administrator is entitled to contest transactions and payments of the insolvent company that prefer certain creditors (preferential transactions).

According to sections 129 to 146 of the Insolvency Act, certain actions (including the granting of collateral to a creditor) taken by the insolvent company and resulting in a direct or indirect reduction of the value of the insolvent estate or in a complication in the enforcement of the rights of the insolvent estates are subject to avoidance rights of the insolvency administrator if the action or actions were taken within certain time periods prior to the filing for insolvency proceedings (suspect periods). The relevant period in which transactions and payments are voidable particularly depends on the underlying motivation of the parties involved and the value of the contingent consideration, as shown by the following examples.

Pursuant to section 130 of the Insolvency Act (congruent cover), the fulfilment of a debt or the granting of collateral, or enabling a counterparty to obtain such fulfilment or collateral, may be contested if it was made:

- in the three months prior to the insolvency filing, provided that at such date the company was illiquid and the other party was aware thereof; or
- after the insolvency filing, provided that at such date the other party was aware of the company's illiquidity or of the fact that the company had filed for insolvency.

This provision enables the insolvency administrator to contest transactions of the insolvent company, irrespective of any right of a creditor to such fulfilment or such security at the time (eg, the right of a creditor to a specific security). Knowledge of circumstances indicating the state of illiquidity of the company, or of the company's application to open insolvency proceedings, is deemed equivalent to actual knowledge of the illiquidity or of the filed petition.

Section 130 of the Insolvency Act does not apply if the underlying security agreement calls for an increase of financial collateral (as defined in section 1(17) of the Banking Act, for example, cash deposits, pledges or fiduciary transfers of securities) to close the gap between the value of the collateral that has already been provided, and the value of the collateral that must be provided under the security agreement (margin collateral).

Pursuant to section 131 of the Insolvency Act (incongruent cover) the fulfilment of a debt, the granting of security the counterparty could not have claimed, or not in such way or at such a time (ie, the creditor was not entitled to claim at the time), under the existing contractual arrangements may be contested if it was made:

- in the month prior to the insolvency filing or after such filing;
- in the second or third month prior to the insolvency filing, provided that at such date the company was illiquid; or
- in the second or third month prior to the insolvency filing, provided that the other party was aware or should have been aware that the action was to the disadvantage of insolvency creditors. Knowledge

that the granting of security is to the disadvantage of other insolvency creditors will be assumed if the creditor knows, or ought to know, at the time of the granting of the collateral, that the debtor will no longer be able to satisfy all of its other creditors in the near future because of the existing financial crisis.

Pursuant to section 133(1) of the Insolvency Act (legal acts wilfully disadvantaging the insolvency creditors), any legal actions taken by a debtor within the 10 years prior to the insolvency filing can be contested by the insolvency administrator, provided that the action was taken by the debtor with the intent of disadvantaging its creditors and the counterparty was aware that the debtor intended to disadvantage its creditors. Knowledge of the debtor's intention will be presumed if the counterparty was aware of the debtor's imminent illiquidity and of the disadvantageous effect of the action on the other creditors. An intention of a debtor to disadvantage its creditors does not require an actual desire of the debtor to disadvantage them. Rather, it will suffice that the debtor recognises that the satisfaction of, or the granting of security to, one creditor can cause disadvantages to its other creditors, in particular reducing the likelihood that its other creditors can be paid (whether in whole or in part) out of the remaining assets.

If no insolvency proceedings have been initiated, transactions and payments of the company may be contested by creditors under the Voidance Act, which provides rights for creditors similar to those of an insolvency administrator in insolvency proceedings.

On 29 September 2015, the German Federal Ministry of Justice issued a (revised) draft reform act on insolvency avoidance law (see Update and trends).

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## Directors and officers

### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The potential for (personal) liability is mainly a risk for the managing directors of a German limited liability company and the members of the management board of a stock corporation. They may have a liability to third parties and the company itself.

In principle, the managing directors of a German limited liability company and the members of the management board of a stock corporation are not liable to third parties for obligations owed by their companies. If they act in their capacity as corporate directors, only the company can be held liable for their actions. Personal liability of a managing director or a management board member can only arise in a few exceptional cases.

#### Liability to third parties generally

Managing directors can be held liable, jointly with the company, for a defective product if the defectiveness results from insufficient supervision or organisation of the production and monitoring process.

Whenever the company is insolvent (illiquid or over-indebted (see question 1)), the managing directors and the management board members have a duty to apply for the opening of insolvency proceedings without delay, but in no event later than three weeks after the date the company became insolvent. If they do not comply with this duty, they can be held liable for damages resulting from the delayed initiation of insolvency proceedings, and may also be liable for a fine or prison sentence of up to three years. Damage claims for the delayed initiation of insolvency proceedings can be asserted by the insolvency administrator (if the underlying contract, from which the claim of a creditor against the debtor results, was concluded prior to the insolvency of the company) or by the creditors (if the underlying contract was concluded after the insolvency of the company, but before insolvency proceedings were actually initiated).

#### Liability towards the company

The managing directors of a German limited liability company and the members of the management board of a stock corporation are required to exercise the diligence expected of a responsible businessman in the conduct of the affairs of the company. If they fail to do so, they will be jointly and severally liable to the company for any resulting damage. The obligation to exercise the diligence expected of a

responsible businessman also includes the duty, if a crisis threatens, to consider all possible remedial steps and, as far as possible, to initiate such measures.

They are required to call a shareholders' meeting if it appears to be in the best interests of the company. A special meeting is required to be called without undue delay if it appears from the annual balance sheet, or from a balance sheet prepared during the fiscal year, that half or more of the share capital has been eroded. A managing director who fails to notify the shareholders in these circumstances may be liable to a prison term of up to three years or a fine.

Whenever the company is insolvent, the managing directors and the management board members have to ensure that the company generally ceases to make payments, unless the payments are consistent with the due care of a prudent businessman (which may, in particular, be the case if the respective payments are essential to uphold the business of the company). Accordingly, they can be held personally liable for payments that result in a reduction of the insolvent estate. In addition, they may also be held personally liable for payments to a shareholder that resulted in the illiquidity of the company, unless such payments were consistent with the due care of a prudent businessman. However, such damage claims are to be asserted by the insolvency administrator in favour of the insolvency estate and, thus, the creditors of the company.

Apart from this, a managing director may also be liable for pre-insolvency actions that are inconsistent with an orderly management of affairs leading to a reduction of the (insolvency) estate. For instance, a prison term of up to five years or a fine may be imposed upon a managing director, who, in the event of over-indebtedness or an impending or actual illiquidity of the company:

- conceals or removes or, in a manner inconsistent with the requirements of an orderly management of affairs, destroys, damages, or renders useless parts of the estate that would belong to the insolvency estate in the event of the institution of insolvency proceedings;
- fails to keep commercial books that he or she is obligated to keep under the law, or keeps or changes such books, in a manner that makes the view of the financial status more difficult; or
- contrary to the requirements of commercial law, prepares balance sheets in a manner that makes the assessment of the financial status more difficult.

A prison term of up to two years or a fine may be imposed upon a managing director who, knowing the illiquidity of the company, grants to a creditor a security or satisfies a debt to which it is not entitled or not entitled in such form or not entitled at such time, and thereby intentionally or knowingly prefers it over other creditors (see question 39).

In principle, these offences are only actionable if the company has stopped its payments, or if insolvency proceedings have been instituted, or if the application for the institution of insolvency proceedings has been rejected for lack of funds.

According to section 69 of the General Tax Code, a personal liability can arise for tax liabilities of the company, provided that such taxes have intentionally or negligently not been paid.

The managing directors can also be personally responsible for financial damages relating to fraud (section 263 of the Criminal Code), breach of trust (section 266 of the Criminal Code) and withholding and embezzlement of the employees' contributions to the social insurance (section 266a of the Criminal Code).

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## Groups of companies

### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

In principle, neither the parent nor affiliated companies can be held liable for the liabilities of subsidiaries or affiliates, unless they have given guarantees or security for the debtor's liabilities. Generally, only the (insolvent) limited liability company is liable to fulfil its obligations unless explicitly agreed otherwise between the shareholder and the company (eg, by entering into a profit and loss transfer agreement) or the shareholder and affiliated companies with the relevant creditors (eg, by providing a guarantee), or both. There is, however, case law on 'piercing the corporate veil', for example, in cases of substantial undercapitalisation of the company or a misuse of the corporate form. The most important category of this case law encompasses capital

maintenance requirements: 'measures of fundamental impairment'. This means that a shareholder must not withdraw the company's assets required for the ordinary course of business, thereby accepting a possible impairment of the company's creditors. In the event of a measure of fundamental impairment, the shareholders – and even the shareholders of such shareholders – can be held personally liable by the insolvency administrator in an unlimited way.

At present, German insolvency law does not specifically address corporate groups and is instead dominated by the principle of 'one entity, one estate, one insolvency process'. Therefore, a court cannot order a distribution of group company assets pro rata without regard to the assets of the individual corporate entities involved.

In the course of the ongoing reform of German Insolvency law, the German Federal Ministry of Justice has issued a draft Act on the Facilitation of the Handling of Corporate Group Insolvencies. This draft bill addresses the current lack of coordination between parallel insolvency proceedings of group companies (see question 29). It does, however, not offer a consolidation of the individual group insolvency proceedings. The draft also contains an explicit rejection of the substantive consolidation of assets and liabilities of group companies.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Repayment claims under shareholder loans and claims resulting from legal actions that are economically comparable to a shareholder loan will generally be classified as subordinated insolvency claims. Also, transactions made by the debtor with insiders or non-arm's-length creditors prior to the opening of insolvency proceedings can regularly be more easily contested, since the German Insolvency Act contains specific avoidance provisions on transactions with related parties (see sections 133(2) and 138 of the German Insolvency Act) and turns partially around the burden of proof to their disadvantage (see sections 130(3), 131(3), 132(3) and 138 of the German Insolvency Act (see questions 39 and 40)).

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

The court order opening insolvency proceedings imposes an automatic stay on unsecured creditors initiating or continuing actions against the company. Unsecured creditors can no longer enforce their rights in legal proceedings outside the insolvency proceedings.

The Insolvency Act does not impose an automatic stay on the enforcement by secured creditors. Creditors, who claim that an asset does not belong to the estate because of a right of segregation, including retention of title creditors are free to enforce their rights against the company. Creditors secured by charges on real estate may enforce such charges irrespective of the insolvency proceeding. The administrator may also initiate such enforcement proceedings, for example, by selling real estate in an auction and paying the proceeds to the security holder. Hence, the creditor and the administrator are both equally and independently entitled to enforcement with respect to real estate.

Creditors with a security interest in moveable property will mainly be prevented from enforcement, which may then only be initiated by the administrator. Moveable assets that are subject to security held by creditors and receivables, which have been assigned for security purposes, will generally be sold by the administrator free and clear of the security and the proceeds of such sale will be paid to the holders of such security, less a handling fee. This shall not affect financial collateral (as defined in section 1(17) of the Banking Act, for example, cash deposits, pledges or fiduciary transfers of securities) and collateral granted to the participant of a securities settlement system (as defined in section 1(16) of the Banking Act). The administrator is not entitled to enforcement if the creditor is still in possession of the moveable asset; in this case the creditor's enforcement right remains unaffected by the opening of the insolvency proceedings.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

German corporate law contains procedures for the dissolution and liquidation of a corporation, which cannot easily be summarised. The cases in which the company may or must be dissolved are set out in the relevant laws. These laws specify additional reasons other than insolvency for the dissolution of the company. At any time, the shareholders' meeting can resolve, with a qualified majority of usually 75 per cent of the votes cast, to dissolve the company.

The commencement of dissolution as such does not cause the company to cease to exist as a legal entity. It merely constitutes the commencement of the company's liquidation by changing the purpose of the company. Once dissolved, the company can no longer pursue the business purpose defined in its articles. Its sole purpose becomes the liquidation of its business, that is, it has to terminate its current business transactions, discharge its obligations, collect its receivables, convert its assets into cash and distribute the liquidation proceeds, if any, to the shareholders.

Generally, the company is liquidated by its liquidators (who are appointed at the shareholders' meeting), except in the case of insolvency, where the insolvency administrator liquidates the company in accordance with the provisions of the Insolvency Act.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Liquidation and reorganisation cases are formally concluded by an order of the insolvency court. As soon as the final distribution has been made, the insolvency court will make an order terminating the insolvency proceedings. As far as reorganisation cases are concerned, the insolvency court orders the termination of the insolvency proceedings as soon as the insolvency plan has been unconditionally approved (ie, an appeal against the order confirming the plan is no longer possible) and any necessary remediation measures to cure the illiquidity or over-indebtedness or both have been implemented in accordance with the insolvency plan (eg, registration of the deb-for-equity swap with the competent commercial register).

If the performance of the plan is to be supervised, an order to that effect will be made together with the order terminating the insolvency proceedings. The insolvency court will then order the termination of supervision when:

- all the claims covered by the plan have been satisfied; or
- three years have elapsed since the termination of the insolvency proceedings and no application to commence a new insolvency proceeding has been filed.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

As far as cross-border insolvencies within the EU are concerned, the EC Regulation on Insolvency Proceedings (Council Regulation (EC) No. 1346/2000) (the EU Insolvency Regulation), applies. On 5 June 2015, the Regulation (EU) 2015/848 replacing Council Regulation (EC) No. 1346/2000 on insolvency proceedings has been published in the Official Journal of the European Union and shall enter into force in all member states except Denmark on 26 June 2017 (the EU Recast Regulation) (see the European Union chapter). Cross-border insolvencies concerning non-EU member states are governed by German international insolvency law, which became effective on 20 March 2003. Both regulations follow the same principles.

Within the EU, the courts of the member state in which the debtor's COMI is situated will have jurisdiction to open main insolvency

proceedings. Generally, foreign insolvency proceedings are recognised automatically and the German assets of the debtor will be subject to the foreign insolvency proceedings. Notwithstanding this, foreign insolvency proceedings will not be recognised if to do so would be incompatible with German public policy. If, pursuant to German international law, the courts of a non-EU member state where the proceedings were commenced do not have jurisdiction over the company, such proceedings will not be recognised in Germany.

If a debtor's COMI is located in a member state of the EU, the opening of secondary proceedings in Germany requires that the debtor has an establishment in Germany. Generally, this is also the case where insolvency proceedings of a non-member state are to be recognised in Germany. Such secondary proceedings encompass only the German assets of the debtor. If foreign insolvency proceedings have already been commenced against the debtor, proof of insolvency is not required for the commencement of the German insolvency proceedings.

Employment relationships with employees working in Germany will still be governed by German law.

Creditors' rights in rem concerning tangible or intangible, moveable or immovable assets that are owned by the debtor and situated in Germany shall not be affected by the commencement of foreign insolvency proceedings.

Although any avoidance is in principle subject to the law that governs the underlying insolvency proceedings, a transaction that, pursuant to the general principles on conflict of laws, is governed by German law, may only be avoided by a foreign insolvency office holder if the transaction may also be avoided pursuant to German law or is ineffective for any other reason.

Foreign creditors are entitled to participate in German insolvency proceedings in the same way as domestic creditors. The foreign creditor is subject to the rules of the Insolvency Act. The Regulation on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters (Regulation of the European Parliament and the Council No 1215/2012 (the Brussels Regulation recast) is also relevant in relation to recognition of foreign proceedings (see the European Union chapter).

Germany has not adopted the UNCITRAL Model Law on Cross-Border Insolvency.

## COMI

### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

The EC Regulation does not contain a definition of 'COMI' but the recitals to it state that the COMI should correspond to the place where the debtor conducts the administration of his or her interests on a regular basis and is therefore ascertainable by third parties. The EC Regulation applies the concept of COMI to each individual debtor and not to a group of companies – which can all have individual COMIs.

In the case of *Interedil (Interedil Srl v Fallimento Interedil Srl and Intese Gestione Crediti SpA (C-396/09))* the ECJ confirmed that COMI must be interpreted in a uniform way in EU member states and by reference to EU law and not national laws. Where a company's registered office and place of central administration are in the same jurisdiction, the registered office presumption set out in the recitals to the EC Regulation cannot be rebutted. Where a company's central administration is not in the same place as its registered office, a comprehensive assessment of all relevant factors makes it possible to establish, in a manner that is ascertainable by third parties, that the company's central administration is located in another EU member state.

Factors that have been held to be relevant to determine a debtor's COMI (in addition to the rebuttable registered office presumption) are: location of internal accounting functions and treasury management, governing law of main contracts and location of business relations with clients, location of lenders and location of restructuring negotiations with creditors, location of human resources functions and employees as well as location of purchasing and contract pricing and strategic business control, location of IT systems, domicile of directors, location of board meetings and general supervision.

The rebuttable presumption that a company's COMI is where its registered office is located has been slightly modified in the EU Recast

Regulation, which states that it is not possible to rely on the rebuttable presumption where a debtor has moved its COMI in the preceding three months (see the European Union chapter).

As regards a corporate group of companies, there is no specific test to determine the COMI. Hence, in general, the parent company and each subsidiary of a corporate group is subject to an individual and entirely separate insolvency proceeding, often at different insolvency courts and under different administrators (see question 29). However, on 30 January 2014, the German government passed an official legislation draft bill that aims to introduce an obligation of the different insolvency courts, insolvency administrators and creditors' committees to cooperate in insolvency proceedings over group entities (see question 29). This draft would introduce – in addition to the venue at each individual debtor's COMI that remains in force – a uniform venue for all companies of the same group (which have their COMI in Germany), providing that one of the debtor companies (or its insolvency administrator) must request such a uniform venue pursuant to proposed section 3a Insolvency Act. The uniform venue constitutes in this case the COMI of the company requesting such uniform venue.

## Cross-border cooperation

### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Generally, German insolvency law allows for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators.

According to article 16 of the EU Insolvency Regulation, any judgment opening insolvency proceedings handed down by a court of a member state which has jurisdiction pursuant to article 3 of the EU Insolvency Regulation (see question 48) shall be recognised in all the other member states from the time that it becomes effective in the state of the opening of proceedings. The judgment opening the proceedings shall, with no further formalities, produce the same effects in any other member state as under this law of the state of the opening of proceedings, unless the EU Insolvency Regulation provides otherwise. However, according to article 26 of the EU Insolvency Regulation, any member state may refuse to recognise insolvency proceedings opened in another member state or to enforce a judgment handed down in the context of such proceedings where the effects of such recognition or enforcement would be manifestly contrary to that state's public policy, in particular its fundamental principles or the constitutional rights and liberties of the individual (*ordre public*).

The concept of an automatic recognition is similar reflected in the Insolvency Act governing international insolvency law for non-EU members. According to section 343 of the Insolvency Act, the opening of foreign insolvency proceedings shall be recognised. However, this shall not apply if the courts of the state of the opening of proceedings do not have jurisdiction in accordance with German law or where recognition leads to a result which is manifestly incompatible with major principles of German law, in particular where it is incompatible with basic rights.

As regards the cooperation between domestic and foreign courts and domestic and foreign insolvency administrators, there are only very few statutory provisions governing such cooperation. According to article 31 of the EU Insolvency Regulation, the administrators of main and secondary proceedings shall exchange all relevant information and shall generally cooperate with each other. The concept of article 31 of the EU Insolvency Regulation is reflected in section 357 of the Insolvency Act governing international insolvency law for non-EU members. Under article 31 of the EU Insolvency Regulation or section 357 of the Insolvency Act, the German administrator is obliged to share all relevant information and documentation with a foreign administrator in order to facilitate an effective and smooth process and the best possible satisfaction of creditors in the insolvency procedures. This would, inter alia, encompass the sharing of information on the insolvency estate, court actions, opportunities to realise the insolvency estate, the registration of claims and avoidance rights.

### Update and trends

During the past year, a hot topic was the restructuring of Germany-based companies by using an English law scheme of arrangement. Between 2010 and 2014, German companies used English law schemes of arrangements successfully to implement financial restructurings and to avoid going into German insolvency proceedings (*Tele Columbus* (2010), *Rodenstock* (2011), *Primacom* (2012) and *Apcoa* (2014)). In the latter case, German-law-governed finance documents were changed to provide for English governed law and for the creditors to submit to the English courts' jurisdiction.

In a number of cases, already the (announced) intention of German companies to use and/or prepare a scheme of arrangement has apparently helped to achieve a consensual solution for the restructuring of financial debts with creditors (eg, *Scholz* (2015/2016), *HC Starck* (2015)).

Schemes of arrangement are (still) in competition with the restructuring measures provided under German insolvency law that, as a consequence of the 'ESUG' (the Further Facilitation of Restructuring Businesses Act), provides, inter alia, for the possibility of a debt-to-equity-swap as part of an insolvency plan, including the option to cram down dissenting shareholders. These restructuring measures have been well received by practitioners as a number of prominent cases have already demonstrated (eg, *Pfleiderer AG* (2012) and *IVG Immobilien AG* (2014)). Whether the outcome of the Brexit vote will make a difference to the number of German companies utilising an English law scheme of arrangement will need to be seen in due course.

A further hot topic relates to the financial restructuring of outstanding bonds under the German Bond Act 2009. Over the past years, a large number of *Mittelstandsanleihen* (mid cap-bonds), which had been increasingly used as an alternative to bank credits, had to be refinanced and/or restructured. Under the German Bond Act 2009, which has replaced the Bond Act dating back to 1899, a bond may be modified (eg, in respect of principal or value) by a majority resolution of the bondholders (75 per cent of the bondholders by amount present at a bondholders' meeting), if the bond provides for such modification. Thus, the Bond Act 2009 can offer an efficient out-of-court restructuring tool that has already been demonstrated in a number of cases (eg, *Solarworld* (2014), *Ekotechnika* (2015) and *Singulus* (2016)).

Against the background of the European Commission's Action Plan on Building a Capital Markets Union (see the European Union chapter), there is a broad discussion among German legislators and insolvency experts:

- whether pre-insolvency proceedings have to be introduced to fulfil the requirements envisaged by the EU or whether the existing German insolvency proceedings that have been introduced by the aforementioned ESUG in 2012 are already sufficient; and

- how such pre-insolvency proceedings should be arranged.

At this stage, it seems not unlikely that a new pre-insolvency proceeding will be introduced, especially because a large number of insolvency experts hold the view that there is a need for such a proceeding.

On 29 September 2015, the German Federal Ministry of Justice issued a revised draft reform act on insolvency avoidance law (after a first draft had been issued in March 2015). The draft aims to reduce legal uncertainty for business transactions mainly caused by the extensive interpretation of the rules by German courts in favour of insolvency administrators. The current legal debate focuses on the insolvency administrator's right to rescind agreements for instalment payments concluded up to a period of 10 years before the application has been filed, provided that the debtor is at least in a state of imminent insolvency and the creditor is aware of this by virtue of external circumstances (see questions 39 and 40). The draft bill proposes to limit the right to set aside legal acts wilfully disadvantaging the insolvency creditors by reducing the period for contesting any payments from 10 to four years.

Furthermore, congruent transactions of the debtor (ie, payments or the provision of collateral by the debtor that the creditor had a right to receive) shall only be voidable if:

- the debtor acts knowing that insolvency is not only imminent but has already occurred; and
- the creditor is aware of this.

Besides, the draft bill provides for privileged treatment of payments by the debtor deriving from an executory title against the debtor obtained in a foreclosure proceeding, and sets out a new regulation on interest payments pursuant to which a debtor of an avoidance claim shall be protected against an excessive interest payment.

The draft bill is still being widely discussed in legal publications and among economists and, thus, stuck in legislative process. However, it is not unlikely that this reform will be implemented in the course of 2016–2017.

In January 2014, the German government passed an official legislative draft bill that should facilitate the handling of group insolvencies (see question 29). The intended bill has been 'pre-packed' with the draft reform act on insolvency avoidance law (mentioned above) and is therefore also in the legislative process.

The reforms to the EC Regulation on Insolvency Proceedings (Council Regulation (EC) No. 1346/2000), which will have an impact on Germany as its provisions will, once in force, be directly binding on Germany, should also be noted. For more information on these reforms, see the European Union chapter.

Although not expressly provided for in the EU Insolvency Regulation or the Insolvency Act, German insolvency administrators are also allowed to enter into protocols in order to establish a contractual framework for the conduct of the various proceedings. Depending on their contents, such protocols require approval by the German creditors' meeting or the creditors' committee.

Under the EU Insolvency Regulation and the Insolvency Act, there are no provisions governing cooperation between domestic and foreign insolvency courts. The UNCITRAL Model Law contains provisions on the cooperation of insolvency courts in international proceedings; these have, however, not been translated into EU or German law. It is undisputed, however, that such cooperation between courts is allowed and some even say that insolvency courts are obliged to cooperate according to the principles established for the cooperation of insolvency administrators. The purpose of such cooperation is, in the first place, to share information in order to avoid jurisdictional conflicts and clarify the financial position of the debtor. Such cooperation is to be handled on an informal basis without formal requests for judicial assistance. Against this background, insolvency courts are also allowed to agree on protocols in order to establish a framework for the different proceedings.

On 30 January 2014, the German government passed an official legislation draft bill that aims to introduce an obligation of the different insolvency courts, insolvency administrators and creditors' committees to cooperate in insolvency proceedings over group entities (see question 29).

New procedures with the aim of facilitating cross-border coordination and cooperation between multiple insolvency proceedings

in different member states relating to members of the same group of companies have been introduced by the EU Recast Regulation (see the European Union chapter).

German insolvency courts have successfully cooperated with foreign insolvency courts and have thus avoided jurisdictional conflicts (in cases such as the insolvency of the PIN Group, where German and Luxembourg courts have been in close contact, or the insolvency of the BenQ Group, where German and Dutch courts have cooperated). There are no reported cases in which German insolvency courts refused to cooperate with foreign courts.

However, in a judgment dated 15 February 2012 (IV ZR 194/09), the German Federal Supreme Court refused to recognise an English scheme of arrangement between the UK-based insurance company Equitable Life Assurance Society (ELAS) and its creditors.

Given the fact that the particular scheme related to an insurance company and, therefore, specific insurance regulation had to be applied, it should however be noted that the court did not decide whether the Council Regulation 44/2001 (the predecessor to the Brussels Regulation recast) could be applied for schemes of arrangements concerning non-insurance companies. However, the court indicated that there were arguments to apply Council Regulation 44/2001 as scheme of arrangements were similar to judgments in the meaning of that regulation. In this connection, it should also be noted that a number of Germany-based companies have successfully used an English law scheme of arrangement during recent years (see 'Update and trends').

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**Cross-border insolvency protocols and joint court hearings**

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- 50** In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

Although German courts have dealt with several well-known cross-border insolvency cases, the German courts have not yet entered into any cross-border insolvency protocols or similar arrangements to coordinate proceedings with courts in other countries. The same applies to joint hearings with courts in other countries. German courts have, however, cooperated with foreign insolvency courts on an informal basis (see question 49).



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# Greece

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Bankruptcy Code (in its current state, Law No. 3588/2007 as amended by Law No. 3858/2010, Law No. 4013/2011, Law No. 4055/12, Law No. 4072/12 and Law No. 4336/2015) is applicable to bankruptcies and reorganisations in Greece. The Bankruptcy Code provides for reorganisation as an alternative to liquidation. Moreover, Greece, by virtue of Law No. 3858/2010, adopted the UNCITRAL Model Law on Cross-border Insolvency. Finally, because Greece is an EU member state, the EC Regulation on Insolvency Proceedings (Council Regulation (EC) No. 1346/2000) (the EC Regulation) also applies. Greek law applies a 'cash flow' insolvency test. A debtor is declared bankrupt in case of present or foreseeable general and permanent inability to meet its financial obligations as they fall due (cessation of payments). Inability is 'general' where it covers all or substantially all of the debtor's financial obligations and 'permanent' where it is not circumstantial and there are no substantial recovery expectations or any financial assistance available either in the form of debt or equity.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The multi-member first instance court of the district in which the debtor has the centre of its main interests (COMI) has exclusive jurisdiction. The court follows the ex parte procedure, hence the court has the authority to review issues beyond what is formally submitted. The court that issues a decision by virtue of which a debtor is declared bankrupt exercises an ongoing surveillance over the bankruptcy proceedings and is authorised to resolve any disputes that arise during the bankruptcy proceedings. However, that court has no authority for any debtor claim against third parties.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Bankruptcy proceedings may be initiated by or against any merchant (individual or legal entity) or any for-profit legal entity.

Public entities and local authorities are excluded from bankruptcy.

Regulated entities are governed as follows:

- insurance companies can be declared bankrupt but not prior to the conclusion of a special winding-up process introduced by Legislative Decree 400/1970 as amended by Presidential Decree 332/2003;
- any credit institution whose licence is revoked by the Bank of Greece, is placed into special liquidation. Greece very recently adopted the provisions of the banking resolution directive (BRD); and
- investment services companies can be declared bankrupt, although any bankruptcy proceedings may be suspended by virtue of article 22 et seq of Law No. 3606/2007, as amended by Law

No. 3756/2009, if the Hellenic Capital Markets Committee revokes such a company's licence, thus leading to an initial stage of distribution of segregated client assets (confusingly named 'special liquidation') and, thereafter, to liquidation or bankruptcy.

Non-merchant individuals are excluded from general bankruptcy proceedings, but Law No. 3869/2010, as amended by Law No. 3996/2011, Law No. 4019/2011, Law No. 4161/2013 and Law No. 4336/2015, has introduced certain protective measures for individuals facing financial distress; such measures are of a temporary nature and subject to various conditions that severely limit their application. While the law may eventually develop into a fully fledged insolvency regime for non-merchants, in its current form it remains focused on softening the impact on individuals of the current economic crisis.

All assets of the debtor are included in bankruptcy proceedings in which all creditors are entitled to participate. Exceptions are provided for individuals such as certain household goods (clothing, food for up to three months, essential furniture, books, musical instruments, etc) and work tools.

Secured creditors can elect to exercise their security thus seeking satisfaction from the proceeds of the secured asset's sale irrespective of the bankruptcy proceedings, unless the assets are closely connected to the debtor's business or production unit or enterprise, in which case such option is suspended until a reorganisation plan is approved or until the creditors' meeting decides on the bankruptcy proceedings to be followed. In any case the aforementioned suspension cannot last more than 10 months commencing from the date the debtor was declared bankrupt. Secured creditors cannot exercise their security if liquidation has been initiated.

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

All commercial undertakings regardless of public or private ownership are subject to the Bankruptcy Code. Specific regulated sectors are subject to special rules as set out above in response to question 3.

## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

There is no specific legislation for institutions that are too big to fail. Nevertheless, Greek law recognises that certain credit institutions play a systemic role and that it is necessary to avoid their resolution or reorganisation. For that purpose, Law No. 3864/2010 set up the Hellenic Financial Stability Fund as an independent agency funded by the state. The purpose of the fund is to maintain the stability of the Greek banking system through capital contributions to systemically important banks that have difficulty maintaining their minimum capital requirements. The same institution also provides funding to cover the funding gaps of credit institutions placed into special liquidation. In connection with such funding, Greece has very recently adopted the banking resolution directive, which includes, among other things, bail-in requirements and other burden-sharing provisions.

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### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

The following types of security are available for immoveable property.

##### Mortgage

This is the basic form of security in relation to immoveable property. In order to create a mortgage, a creditor must hold a title provided by law, final court decision or a notarial deed. A mortgage is perfected by its registration in the Land Registry.

##### Prenotation of mortgage

This is the most common form of security on real property and is created by a court order in the nature of an injunction. It can be viewed as a conditional mortgage that can be converted into a full mortgage upon the debtor's default with retroactive effect as of the issuance of the prenotation order. Prenotations are far more common than mortgages because court fees are significantly lower than the notarial fees that would be payable for the mortgage deed.

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### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The following types of security are available for moveable assets:

- Pledge: this is the most common form of security. A pledge on a moveable asset ensures the preferential satisfaction of the creditor through a forced sale of that moveable asset in execution proceedings. A pledge requires physical delivery of the moveable asset to the pledgee.
- A chattel mortgage (articles 1 and 3 of Law No. 2844/00) (also non-possessory pledge): a chattel mortgage allows the debtor to retain possession and use of the moveable asset, and to freely dispose of it, but it attaches to the asset and ensures that the creditor is preferentially satisfied through the asset's forced sale, following the commencement of execution proceedings.
- Floating charge (article 16 of Law No. 2844/00): a floating charge enables the debtor to deal with (and dispose of) the charged assets (as specified in the agreement) in the ordinary course of business until the occurrence of either a default or an agreed event that causes the floating charge to crystallise. Following crystallisation, a floating charge becomes a fixed charge (similar to a pledge) attaching to whatever moveable assets are available at that time.
- Retention or fiduciary transfer of ownership: this allows the creditor, until fully paid, to retain ownership of property or have ownership of property transferred to him, but not to dispose of that property. This occurs in two situations:
  - it is common in sales on credit for the seller to retain ownership until full payment of the agreed upon consideration; and
  - a debtor can conditionally transfer, to the creditor, the ownership of the moveable assets to secure performance of its obligations. Once the obligations are fulfilled, ownership reverts automatically to the debtor. However, if the debtor defaults the creditor must auction the moveable asset and satisfy his claim through the proceeds of the auction.
- Third-party structure: this can include the delivery of a moveable asset to a custodian. However, because Greek law does not recognise the trust concept, the third party that will take delivery of the asset may not also acquire title in trust for the debtor and creditor. Realisation of the asset must be done under the rules for realising a pledged asset, namely, through a public auction.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Unsecured creditors can individually attempt to recover their debt through ordinary legal proceedings. The creditor can enforce its rights after obtaining an executory title against the debtor (article 904 of the Code of Civil Procedure). A creditor with an executory title can seize any of the debtor's assets, proceed to their forced sale (through

an auction) and claim satisfaction from the sale proceeds. Assets sold through a forced sale are relieved from all encumbrances and creditors that have security on those specific assets along with creditors that enjoy a statutory priority are satisfied in priority to other creditors.

Unsecured creditors prior to and until obtaining an executory title can apply for an interim order, for a prenotation of mortgage over the debtor's immoveable assets or a conservative attachment over the debtor's other assets. Such proceedings will require at least three and may take as long as eight months and will require, among other things, proof of imminent danger.

No special procedures apply to foreign creditors.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Any debtor that has ceased payments in a general and permanent way must file a bankruptcy petition within 30 days following cessation of payments. Cessation of payments is defined by the statute as a general and permanent inability to meet monetary obligations as they become due and payable. Any debtor that is in imminent financial distress, in the sense that it foresees upcoming liquidity problems and potential default on its payments, amounting to a cessation of payments, may also file a bankruptcy petition.

In principle, once a debtor is declared bankrupt, a bankruptcy administrator will be appointed to manage the debtor's assets and affairs. In exceptional circumstances, a debtor may remain in control of its assets and affairs. The court – following a petition by the debtor and to the extent this is to the benefit of the creditors and the creditors' committee agrees – may permit the debtor to remain in possession and administration of its assets always along with the bankruptcy administrator's cooperation. To our knowledge, to date Greek courts have addressed an application to maintain the debtor in possession only once (Decision No. 747/2009 of the Multi-member First Instance Court of Athens); in that case the application was rejected as not being in the creditors' interests.

After a debtor is declared bankrupt, all enforcement actions and proceedings against the debtor are automatically suspended. Secured creditors' rights arising from existing security are not affected but, in practice, realisation of the assets is difficult as enforcement will be impeded in the event that the assets are closely connected to the debtor's business or production unit or enterprise, after a reorganisation plan is approved or when the creditors' meeting decides over the bankruptcy proceedings that will be followed, in which case article 26 of the Bankruptcy Code provides for an automatic suspension of all actions and enforcement procedures. Any enforcement proceedings attempted during the suspension are null and void. If the creditors' committee decides to sell the debtor's assets as a whole, the moratorium lasts until the sale is concluded.

One of the important consequences of filing a petition on the basis of an imminent cessation of payments is that the court, if convinced, will set the date of cessation of payments as the date on which bankruptcy is declared; accordingly there will be no suspect period and no threat of transactions being set aside by the bankruptcy administrator.

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Any creditor can file a petition to have its debtor declared bankrupt. Insofar as the effects of an involuntary liquidation are concerned, the process follows the same steps as noted in question 9, the sole exception being that the court does not have the discretion to leave the debtor in possession.

A procedure similar to involuntary bankruptcy was introduced as part of the reform of pre-insolvency proceedings. This procedure, known as special liquidation, applies to debtors who have or will have a general and permanent inability to meet their financial obligations as they fall due. Special liquidation can be decided at the application of creditors who represent at least 20 per cent of the total claims against the debtor. The creditors must also submit a statement of the proposed special liquidator with regard to the acceptance of the assigned duty as well as the special liquidator's report with regard to the special liquidation proceedings that will be followed. If the application is accepted,

the court will appoint the proposed liquidator to continue the business as a going concern and to conduct a public auction for its transfer to the highest bidder as a going concern. If there is more than one proposed liquidator, the court will appoint the most suitable.

The acceptance of the special liquidation application results in the automatic stay of all individual enforcement actions against the debtor throughout the process of the special liquidation.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The Bankruptcy Code provides for two proceedings that are relevant to the restoration of a failed enterprise to financial health; once the recovery procedure that precedes bankruptcy. The second, the reorganisation plan, is considered after the declaration of bankruptcy.

#### Pre-bankruptcy recovery procedure

A debtor either in cessation of payments or in a situation of imminent cessation of payments can apply to the court for the opening of the recovery procedure to enable the debtor to negotiate an agreement with its creditors representing a majority of 60 per cent of the total claims, 40 per cent of which should be secured, or to ratify an agreement already reached with such qualified majority of creditors. In addition, any debtor that is not in cessation of payments or in a situation of imminent cessation of payments can be subject to the recovery procedure, provided that the court considers it probable that the debtor will become insolvent, and insolvency can be lifted through implementation of the recovery procedure.

The creditors can be approached ad hoc or through a committee to which all shall be invited to participate. The debtor may seek the appointment of a mediator to assist with the negotiations (and shall nominate a suitable candidate to the court) or even a special administrator to take over the management of the debtor and the control of its assets pending such negotiations. The agreement may consist of a pre-pack sale of all or part of the business, a disposition of assets, a debt-equity swap, or a change of the term of existing obligations, such as a write-down of the debt, extension of the repayment date, alteration of the interest rate or replacement of the obligation to pay interest by the obligation to provide the creditor with a share of the profits; such changes to liabilities may also be accomplished through a refinancing of existing debt or through the issue of a bond loan that may also include a convertibility feature.

Upon filing for initiation of the recovery procedure and until the termination of the procedure (meaning the ratification of the agreement, or the rejection of the relative application, or the expiry of the four-month period as extended by the Bankruptcy Court) a moratorium on all enforcement actions may be provided by the bankruptcy court as a preliminary measure. Any moratorium on all enforcement actions awarded will automatically prevent any transfer of the debtor's immovable property and equipment. In any case, the suspension will be granted if creditors representing a majority of 30 per cent of the total debts, 20 per cent of which should be secured, consent. The Bankruptcy Court will examine whether the recovery agreement will be achieved, as well as whether the debtor's bankruptcy will be prevented (ie, both conditions must be met).

There are three main criteria for the ratification of an agreement reached by the debtor and the qualified majority of creditors as set out above. First, it must result in a viable business and lift the debtor out of cessation of payments (or prevent it from reaching this state). Second, it must not leave any non-consenting creditors in a less favourable position than they would be in bankruptcy liquidation. Third, each non-consenting creditor may not be treated less favourably than any other creditor of the same rank or priority.

The Bankruptcy Court will not examine the debtor's viability if the following conditions are met:

- contracting creditors agree with the content of the business plan;
- the recovery agreement contains listing of contracting and non-contracting creditors, the claims of which are expected to be affected from the materialisation of the recovery agreement; and
- the recovery agreement along with the business plan were served to all non-contracting creditors, the claims of which are affected from the recovery agreement.

A ratified agreement binds all non-consenting creditors (cram-down effect).

#### The reorganisation plan

Any debtor, within four months of being declared bankrupt, or any debtor who is filing a voluntary bankruptcy petition, can propose a reorganisation plan. In exceptional cases the four-month period may be extended by up to three months. The bankruptcy administrator is also entitled to submit a reorganisation plan immediately after the four-month period has elapsed, and within three months of such expiration.

The main effects are as follows:

- This is a novel proceeding for Greek law and has hardly been tested in practice. The statute seems to permit the development of a debtor-in-possession insolvency proceeding, as the court, upon receiving a voluntary insolvency application and a plan that provides for the continuation of the debtor's business, may decide to allow the debtor to maintain control of the business along with the bankruptcy administrator's cooperation.
- Upon filing for declaration of bankruptcy and until the grant of the relative order, a moratorium against all enforcement actions (including the involuntary grant of security over assets) may be provided by the competent court as a preliminary measure.
- The declaration of bankruptcy puts into immediate effect a moratorium on all enforcement actions by unsecured creditors. Secured creditors cannot continue pursuing their claims against the secured assets that are closely connected to the debtor's business or production unit or enterprise until the reorganisation plan is approved. Any enforcement procedures attempted during the suspension are null and void.
- The ratified reorganisation plan is binding erga omnes (such cram-down includes the dissenting and non-participating creditors).

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Under the Bankruptcy Code, creditors cannot initiate an involuntary reorganisation plan. The only alternative to bankruptcy available to creditors is to file for a sale of the debtors' business as a going concern under the special liquidation proceeding.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Companies and merchants are obligated to file for bankruptcy within 30 days following cessation of payments. Failure to file for bankruptcy in a timely manner will cause company representatives to be held personally liable for damages caused to creditors by trading while insolvent. Accordingly, the creditors' compensation is restricted to unpaid debts created during the period between the date the bankruptcy petition should have been filed and the date the company was actually declared bankrupt. The aforementioned claims can be pursued only by the bankruptcy administrators and not by creditors who suffered the damage.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

#### Recovery procedure

No conditions or restrictions are set by law on the debtor's conduct of business. No conditions apply to the use or sale of assets and to creditors who supply goods or services. The creditors can contest initiation of the recovery procedure. The court intervenes in key parts of the

recovery process. Initially the court determines whether a moratorium will be imposed (excluding the pre-packaged recovery, in which case an automatic moratorium is imposed) as well as the form of the moratorium or the conditions that will run with it. Any moratorium regarding enforcement actions against the debtor automatically prevents transfer of the debtor's immoveable property and equipment. Moreover, the court decides on the opening or not of the recovery procedure and finally ratifies the agreement. The court may appoint a special administrator to control the debtor's assets or to perform specific actions or to oversee performance of the recovery agreement. Creditors that, pursuant to the recovery agreement, supply credit, goods and services to the debtor for the continuation of its business activities, (in the event that the recovery agreement is terminated), are ranked as first-class general preferential creditors for the value of the credit, goods and services provided, superseding all other creditors. Furthermore, creditors that supplied goods and services during the period after initiation of the recovery procedure and until ratification of the recovery agreement, in case the recovery agreement is terminated, are also ranked as first-class general preferential creditors superseding all other creditors.

### The reorganisation plan

The right to manage and transfer the debtor's assets passes to the *syndikos* (bankruptcy administrator) after the commencement of the insolvency proceedings. Directors and officers, however, continue to exercise the rights that are irrelevant to the administration of the insolvency estate. For instance, the board of directors of a *société anonyme* and not the bankruptcy administrator retains the authority to convene the general assembly of the shareholders of the company in order to approve the annual financial statements, while it is the board of directors that is solely competent to certify the payment of the share capital. In exceptional circumstances, a debtor may remain in control of its assets and affairs. The court – following a petition by the debtor and to the extent this is to the benefit of the creditors and the creditors' committee agrees – may permit the debtor to remain in possession and administration of its assets, always with the bankruptcy administrator's cooperation, and subject to being recalled if that is held to serve the creditors' interests. Sale of assets or equipment is possible after ratification of the reorganisation plan and subject to its provisions.

In both schemes, creditors who supply new credits following and in connection with a ratified recovery agreement or a ratified reorganisation plan in case such agreement or plan is terminated, become first-ranked general preferential creditors superseding all other creditors.

The bankruptcy administrator oversees performance of the reorganisation plan and reports to the creditors' committee every six months.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

##### Recovery procedure

The court can, and frequently does, order an interim moratorium on all enforcement actions against the debtor for the interval between the filing of the petition with regard to the opening of the recovery procedure and the judicial ratification of the debtor-creditors' agreement, or the rejection of the relative application for ratification, or the expiry of the up to four-month period – which can be extended by the Bankruptcy Court – following the publication of the decision ordering the commencement of the procedure. In principle, the interim measures may be imposed on creditors' claims that arose prior to the opening of the recovery procedure. Exceptionally the court may extend the suspension on creditors' claims that arose *ex post facto* to the commencement of the recovery procedure as well. Any moratorium regarding enforcement action automatically prevents transfer of the debtor's immoveable property and equipment. It is also worth noting that, unless the court decides otherwise, a provisional moratorium will not prevent the enforcement of employee claims.

The creditors' enforcement rights arising from any financial collateral arrangement, or from any close-out netting provision, or any creditor's right to terminate the lease agreement if the debtor is in arrears for at least six monthly payments, are excluded from the suspension.

As already noted, the suspension will be granted if creditors representing a majority of 30 per cent of the total debts, 20 per cent of which should be secured, consent. The Bankruptcy Court will examine whether the recovery agreement will be achieved, as well as whether the debtor's bankruptcy will be prevented. The same applies to the pre-bankruptcy special liquidation procedure.

At the time when the pre-packaged recovery agreement is filed for ratification, there is an automatic moratorium on all individual and collective enforcement measures against the debtor. Such a moratorium cannot exceed a four-month period.

### Reorganisation plan and liquidation proceedings

Once the debtor is declared bankrupt, all unsecured and general preferential creditors are barred from enforcing their rights and remedies against the debtor.

Secured creditors can continue to pursue their claims against the secured assets unless the secured assets are closely connected to the debtor's business or production unit or enterprise, until either a reorganisation plan is approved or the creditors' committee decides whether the bankruptcy administrator will continue the debtor's commercial activities for a certain period of time; lease the business; sell the company as a going concern through a public auction; or proceed to the piecemeal sale of the debtor's assets. In any case, the suspension cannot last more than 10 months from the day the debtor was declared bankrupt. If the creditors approve the sale of the debtor's assets as a whole, the suspension lasts until the sale is concluded, for which the law does not set a deadline.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

There are no specific provisions with regard to funding either obtained prior to judicial ratification of a reorganisation plan or prior to the submission of a recovery agreement for judicial ratification or upon commencement of liquidation proceedings.

Loans or credit provided pursuant to a recovery agreement or a reorganisation plan or credit provided after the submission of a recovery agreement for judicial ratification are, however, ranked as first-class general preferential claims, superseding any other pre-existing claim, but that priority status is conditional on the ratification of the plan.

### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

The creditors have the right to offset their claims against debtor's claims provided that their claims became due and payable prior to the debtor's bankruptcy. The bankruptcy court may order the temporary suspension of creditors' right to set-off.

### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

Until the ratification of a reorganisation plan or a decision of a creditors' committee deciding for debtor's liquidation any sale of assets is forbidden without prior permission by the reporting judge granted under exceptional circumstances. Any sale of the debtor's assets in case of a reorganisation plan can be contemplated after ratification of the reorganisation plan, pursuant to its provisions. Liquidation pursuant to a creditors' committee decision is performed through a public auction by submission of sealed offers. The purchaser acquires the assets 'free and clear' of claims. 'Stalking horse' bids are not possible because all sales are conducted by means of a public auction in which all bidders

participate on identical terms. Bilateral negotiations even prior or after are excluded. Credit bidding is permitted under limited circumstances, such as when the debtor's moveables are acquired by the debtor's creditor who commenced compulsory execution proceedings provided that no other creditor announced any claim against the debtor.

With respect to sale of assets during pre-bankruptcy procedures the following applies. Transfer of specific assets or the sale of the debtor's entire business may be the object of the recovery agreement. The purchaser in such cases acquires all or part of the debtor's assets and, if provided by the recovery agreement, all or part of the debtor's liabilities. Liabilities are:

- satisfied by the sale price;
- written off;
- converted into equity (debt-equity swaps); or
- remain as part of the debtor's obligations.

Until ratification of the recovery agreement, assets can be transferred in case there is no moratorium in place and subject to rules regarding fraudulent conveyances and provisions regarding transfers during the suspect period.

In the case of sale of all assets pursuant to a pre-bankruptcy special liquidation, the purchaser acquires all assets free and clear of all claims.

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### Intellectual property assets in insolvencies

**19** May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

There are no special provisions regarding IP rights and the rules generally applicable to the performance of contracts apply. Such law permits the operation of ipso facto contractual clauses: accordingly, insolvency may be agreed to constitute a contractual event of default. If a contract is not terminated, the bankruptcy administrator can elect to continue its performance. However, upon termination the estate is not entitled to the benefit continuous use of the IP.

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### Personal data in insolvencies

**20** Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

There are no special provisions regarding personal information or customer data in the Greek Bankruptcy Code (GBC), and the restrictions generally applicable to personal data, apply. To the extent that any type of information or customer data is deemed to be personal data, any use thereof, including transfer to a purchaser, as, for instance, in case of transfer of any business as per the provisions of a ratified recovery agreement, is subject to the provisions of Law No. 2472/1997.

As a general rule, when collecting and processing personal data, data controllers bear obligations towards the data subjects and the Data Protection Authority.

Personal information or customer data may be used during any insolvency and pre-insolvency procedure provided that such use is compatible with the purposes for which they were originally collected by the insolvent or pre-insolvent company. Any use of personal data must comply with the principles of proportionality, data quality, fairness and necessity, meaning that personal data must be:

- adequate and not excessive in relation to the purposes for which they were collected and/or further processed;
- kept accurate and up-to-date; and
- retained for the time period that is necessary for the purposes for which they were collected.

New consent is not required on the condition that personal data is used for the purposes for which it was originally collected. Any consent must meet the requirements of the law, that is, must be freely given, unambiguous, specific and informed.

Regarding the transfer of such information to a purchaser, such transfer shall be in principle compliant from a data protection law

perspective provided that the data subjects have been originally informed that their personal data shall be passed on to other organisations and in principle consented thereto. This may be achieved through appropriate terms in the contractual arrangements entered into between the insolvent and pre-insolvent company and the data subjects.

Even if the data subjects have been appropriately informed about the transfer of their personal data, the transfer is still subject to the principles set by Law No. 2472/1997. Having said that, personal data must be used by the purchaser for the purposes for which it was originally collected. Personal information should not be used in a way that would be outside of the reasonable expectations of the individuals concerned. If the purchaser intends to use personal data for any other purposes than the purposes for which it was originally collected, consent for the new purpose or purposes is required from each data subject.

Following the transfer of data of personal data, the purchaser shall be deemed to be a controller and shall bear the respective obligations towards the subjects and the Data Protection Authority. Therefore, the purchaser will have to inform the data subjects about the change of the controller and provide them information regarding the enforcement of their rights under Law No. 2472/1997 (right of access, right to object, etc) and notify this change to the Data Protection Authority. Where the transfer of personal data, involves sensitive personal data, such transfer may also be subject to prior authorisation by the Data Protection Authority.

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### Rejection and disclaimer of contracts in reorganisations

**21** Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

In general, any contract may provide for a termination right, in the event that the counterparty is declared bankrupt.

The GBC provides for the maintenance of enforceability of any mutual contract not having been performed by either party in full at the time bankruptcy is declared, unless otherwise provided by the contract. More specifically, the bankruptcy administrator has the right to opt for the performance of the aforementioned contract. If the bankruptcy administrator fails to act, the counterparty can request that the liquidator decide within a reasonable deadline whether he or she opts for the performance of the contract. If the bankruptcy administrator does not reply within the established deadline, or if he or she refuses to perform the contract, then the counterparty is entitled to repudiate the contract and claim for damages.

Contracts of a continuous nature may provide for a termination right in the event of a party's bankruptcy. In the absence of such a term, the GBC establishes the maintenance of their enforceability. In that case, provided that the breach of the contract constitutes an event of default, the contract may be terminated, regardless of the debtor's insolvency.

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### Arbitration processes in insolvency cases

**22** How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Arbitration cannot be used in bankruptcy proceedings in Greece. Courts have held that an arbitration clause lapses after a debtor is declared bankrupt. However, theorists have recently proposed that a bankruptcy administrator should be considered competent to appoint arbitrators, continue arbitration or agree on an arbitration clause.

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**Successful reorganisations**
**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

A pre-bankruptcy recovery agreement will be judicially ratified if:

- it is signed by creditors representing a majority of 60 per cent of the total claims, 40 per cent of which should be secured. The required consent of the creditors' majority may arise from a decision of a creditors' assembly that requires at least a 50 per cent quorum and a majority of 60 per cent of the total claims represented, 40 per cent of which should be secured;
- it renders the debtor viable;
- non-signatory creditors receive as least as much as they would receive through enforcement proceedings or bankruptcy liquidation;
- it does not violate any mandatory legislation, such as competition law, or is the result of fraud conducted by the debtor or any creditor or any third party;
- creditors of the same class are treated equally and any exceptions are justifiable by important business or social reasons; and
- it lifts the debtor out of cessation of payments.

The Bankruptcy Court will not examine the debtor's viability if the following conditions are met: contracting creditors agree with the content of the business plan; the recovery agreement contains listing of contracting and non-contracting creditors, the claims of which are expected to be affected from the materialisation of the recovery agreement; and the recovery agreement along with the business plan were served to all non-contracting creditors, the claims of which are affected by the recovery agreement, as for instance, when the recovery agreement provides for their write-off or for an extension of the repayment date.

**Reorganisation plan**

The proposed reorganisation plan must include:

- information relating to the current financial situation of the debtor;
- at least one proposed form of reorganisation; and
- information relating to payments to creditors. The latter is subject to one restriction:
  - the proposed debt settlement must not prejudice creditors' classification.

The plan must mandatorily provide for secured creditors, general preferential creditors, unsecured creditors and subordinated creditors. Employee claims constitute a particular class. Claims of unsecured creditors that are of diminished value may be classified separately. Within a particular class, more than one group of creditors may be provided. The plan must provide equal treatment among creditors of the same class, or among creditors of the same group.

The court initially examines and pre-approves the plan. Following judicial approval of the plan, the creditors vote on the plan and, finally, if a majority of creditors representing 60 per cent of the debtor's debt, at least 40 per cent of which represent secured debt, approves, the plan is filed for judicial ratification.

There is no provision forbidding release of non-debtor parties from liability either in a recovery agreement or a reorganisation plan. With respect to a recovery agreement, the court might not ratify the agreement if such term is considered as affecting the interests of non-signatory creditors.

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**Expedited reorganisations**
**24 Do procedures exist for expedited reorganisations?**

Yes. A (pre-pack) recovery agreement can be executed and filed for ratification without first petitioning to initiate negotiations with creditors under the protection of stay of executions.

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**Unsuccessful reorganisations**
**25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**
**Recovery procedure**

The bankruptcy court will order the opening of the recovery procedure for a period of up to four months. Such a period can be extended by the Bankruptcy Court, but the total duration of the process cannot exceed a 12-month period. If the court determines that either an agreement will not be reached, or the debtor will not become viable, or the non-consenting creditors will receive less than they would have in case of an enforcement procedure or liquidation, the court will reject the debtor's application.

The court's decision is subject to appeal.

At a subsequent stage, the bankruptcy court will not ratify a voluntary reorganisation (recovery) agreement if:

- the debtor is not likely to become viable;
- the non-signatory creditors will receive less than they would have in case of an enforcement procedure or liquidation;
- the recovery agreement violates mandatory legislation, such as competition law, or is the result of fraud conducted by the debtor or any creditor or any third party;
- creditors of the same class are not treated equally; and
- through the proposed recovery, the cessation of payments is not lifted. In that case, provided that there is a pending application for the declaration of bankruptcy, the court declares the debtor bankrupt.

The court's decision is subject to appeal. A new application with regard to the opening of the recovery agreement cannot be filed prior to the lapse of a three-year period. Such a time limit does not refer to the submission of a pre-packaged recovery agreement. Provided that a recovery agreement is not concluded within the attributed period, the recovery process is ipso jure terminated.

**Reorganisation plan**

A proposed reorganisation plan prior to its approval by creditors is subject to examination by the bankruptcy court. The bankruptcy court may reject the plan if:

- the formalities with regard to the mandatory features of the reorganisation plan and the classification of creditors are not met (see question 23);
- it is unlikely that the plan will be accepted by creditors or ratified by the court; or
- creditors' claims and any third party's claims to which the plan is referred may obviously not be able to be satisfied.

The decision that rejects the plan is not subject to appeal. However, the debtor and the bankruptcy administrator are entitled to file an amended or a totally new reorganisation plan within the statutorily established time periods.

Following judicial pre-approval, the creditors' meeting will vote on the plan. A reorganisation plan will be accepted if a majority of creditors representing 60 per cent of the value of the total debts, no less than 40 per cent of which are secured, vote in favour of it. The debtor has the right to withdraw prior to creditors' voting. In that case, the reorganisation proceedings are cancelled.

Once the plan is accepted, it requires judicial ratification. The bankruptcy court will not ratify the plan if:

- the formalities with regard to the voting and creditors' majority are not met;
- the acceptance of the plan is the consequence of a malicious act perpetrated by the debtor, any creditor, the bankruptcy administrator or any third party;
- rejection is dictated by public interest; or
- the plan prejudices the interests of dissenters.

In principle, and regarding both aforementioned procedures, a debtor's default in performing an undertaken obligation does not affect the continuing force and effect of the plan or agreement, unless it evidences that the debtor has become incapable of complying with its obligations under the plan or the agreement. In all other cases, if the debtor

defaults as to a specific obligation, the non-defaulting counterparty may exercise its individual rights under the law and the contract and, if appropriate, may file for the debtor's involuntary bankruptcy.

### Insolvency processes

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

All decisions with regard to bankruptcy proceedings are published in the Bulletin of Judicial Publications of the Jurists' Pension Fund. All creditors are invited in writing by the bankruptcy administrator to announce their claims within a time period of one month after the publication of the decision that declared the debtor's bankruptcy in the Bulletin of Judicial Publications of the Jurists' Pension Fund.

The most significant creditors' meetings are:

- the creditors' meeting that decides on the continuation of the business activities, or the sale of all or substantially all of the debtor's assets or the piecemeal liquidation of the debtor's estate; and
- the creditors' meeting for voting on the reorganisation plan.

The bankruptcy administrator must submit to the creditors' meeting a report with regard to the debtor's current financial situation, the reasons that led to its bankruptcy, the prospects of continuing business activities and the possibility of adopting a reorganisation plan. The bankruptcy administrator oversees the performance of the ratified reorganisation plan and every six months submits a report to the creditors' committee, for a three-year period unless the plan provides differently.

The GBC does not provide for the right of creditors to pursue the estate's remedies against third parties.

A recovery agreement can extend the benefit of any diminution of the debtor's liability to co-obligators and guarantors. A similar provision is not given in respect of a reorganisation plan.

### Enforcement of estate's rights

**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

No, the GBC does not permit the estate creditor to pursue its claims if the bankruptcy administrator has no assets to pursue a claim. There is no express prohibition of a financing of such claims by creditors secured by the claims.

### Creditor representation

**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

The creditors' meeting may pass a resolution upon the appointment of a creditors' committee. The committee consists of three ordinary and three substitute members. One each of the ordinary and substitute members are selected from the class of secured creditors, general preferential and unsecured creditors.

The creditors' committee is assigned with the general duty of supervising the progress of bankruptcy proceedings and assisting the bankruptcy administrator during the performance of his or her duties. The committee may be assigned particular duties, such as:

- filing a petition for the alteration of the time period during which the payments were suspended;
- appointing a proxy to whom the notices will be served;
- filing an application for the preservation of employment until the judicial ratification or rejection of the reorganisation plan;
- objecting to the settlement concluded by the bankruptcy administrator with regard to debtor claims against third parties and vice versa;
- filing an application for the removal and replacement of the bankruptcy administrator;

- submitting a report to the bankruptcy court insofar as the bankruptcy administrator's fees are concerned;
- objecting to the way business activities are continued; and
- intervening in challenges of creditors' claims.

The Bankruptcy Code does not preclude the creditors' committee from retaining external advisers at its own expense.

### Insolvency of corporate groups

**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

The GBC does not provide for the bankruptcy of groups of companies. More specifically, it does not provide for any procedural or substantive (pooling of assets and liabilities) consolidation in case of a bankrupt enterprise group. However, each company member of the group is subject to distinct bankruptcy proceedings. This is in accordance with the fundamental principle of separate corporate personality of each company member of a group. The parent company is not held liable for the corporate debts incurred by any of its affiliates. Nevertheless, the COMI concept that is used as a criterion for the determination of the competent bankruptcy court may centralise the bankruptcy proceedings of a corporate group before the same court. This is the case when the subsidiary's COMI coincides with the parent's COMI. In this case, the bankruptcy court, at its absolute discretion, may appoint the same bankruptcy administrator to conduct the bankruptcy proceedings of the parent company and its affiliate.

### Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

As a general rule, the decisions issued by the bankruptcy court are subject to an appeal and appeal in cassation unless otherwise provided in the GBC. However, the decisions of the bankruptcy court with regard to the appointment or replacement of the reporting judge and the bankruptcy administrator are excluded from the above-mentioned judicial review.

The court decision that declares the debtor bankrupt, the decision upon the challenge exercised by any creditor who failed to announce its claims within the statutorily established time period and that aims at the verification of the creditor's claims by the bankruptcy court and the decision upon a lawsuit exercised by the bankruptcy administrator or any creditor in order to set aside transactions that were made during the suspect period are subject to an appeal and appeal in cassation.

However, the decision that opens the recovery process and the decision that ratifies the recovery agreement may not be appealed. Solely the decision that rejects the application for the commencement of the recovery process and the application for the ratification of the recovery agreement may be appealed.

With regard to the special liquidation process, the decision that opens the process may not be appealed. Only the decision that rejects the application for the opening of the special liquidation process is subject to an appeal. However, the decision that either ratifies or not the special liquidator's report with regard to the transfer of the business as a going concern to the highest bidder is not subject to any appeal.

Insofar as the reorganisation plan is concerned, the decision that rejects the reorganisation plan and that is issued at the stage of the judicial pre-approval may not be appealed. However, at the stage of judicial ratification of the plan, the decision that either ratifies or rejects the plan is subject to an appeal.

In case of realisation of the debtor's estate as a going concern, the decision by virtue of which the value of the business and the first bid price are determined is not subject to an appeal and appeal in cassation. The same applies when the court approves the transfer agreement that is concluded with the highest bidder.

Each stage of the public auction procedure that is conducted for the sale of the debtor's estate either as a whole or for the piecemeal liquidation, may be challenged by anyone who has a lawful interest with an opposition lodged before the bankruptcy court. The court order upon the opposition is subject to an appeal. The same applies in case of an opposition against the distribution list drafted by the bankruptcy administrator.

Finally the decision that orders the discharge of the debtor is subject to an appeal.

In all aforementioned cases in which the exercise of an appeal is provided within the GBC, no special permission must be given to the appellant. However, the appellant must pay a fee of €500, otherwise the court of appeal will not examine the application.

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## Claims

### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

The bankruptcy liquidator invites all creditors that are included within the list provided by the debtor to announce their claims within one month of the public notification of the decision that declared bankruptcy. Creditors that fail to announce their claims within the statutorily established time frame may seek judicial verification of their claims through filing a petition before the bankruptcy court.

Three days following the lapse of the time period that is established for the announcement of creditors' claims, the bankruptcy administrator must verify each creditor's claim before the bankruptcy judge. At this stage, it is likely that a creditor's claim may be challenged by the debtor, the bankruptcy administrator (*syndikos*) or other creditors whose claims have temporarily or finally been accepted. The judgment upon admission or rejection of one's creditor claim is subject to an appeal.

The GBC contains no specific provisions for the transfer of creditors' claims. Any transfer of claim can take place according to provisions of the Civil Code on assignment.

The GBC recognises claims for contingent or unliquidated amounts. Conditional claims are announced (submitted) for verification as if they were not conditional. In case of a condition subsequent, the creditor must return any distribution upon fulfilment of the condition. In case of a condition precedent, the creditor will be ranked but receive payment either by placing a guarantee or upon fulfilment of the condition. Finally, at the time bankruptcy is declared, the non-due and payable creditors' claims, excluding the secured creditors' claims, are deemed to be due and payable. The secured creditors' claims are payable at their actual expiry date.

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## Modifying creditors' rights

### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The Bankruptcy Code does not provide for any change to the classification of creditors' claims. Any involuntary change of priority would probably be deemed unconstitutional as a violation of article 17 of the Greek Constitution.

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## Priority claims

### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

The major privileged claims are the following (in order of seniority).

#### Loans or credit provided pursuant to a ratified recovery agreement or a ratified reorganisation plan

The following creditors' claims, which are ranked at the same class:

- unpaid employee remuneration incurred in the two years prior to bankruptcy being declared and employment termination compensation, regardless of when it occurred;

- lawyers' fees that date up to six months prior to the declaration of bankruptcy, and claims for compensation of salaried lawyers because of termination of their contract for a salaried mandate, regardless of the time it arose;
- social security contributions that arose until the declaration of bankruptcy; and
- claims of the state arising from value added tax (VAT) and its surcharges.

#### Other claims of the state excluding claims arising from VAT

After deducting bankruptcy expenses and the bankruptcy administrator's remuneration, secured creditors are paid out of 65 per cent of the sale proceeds. General preferential creditors are paid out of 25 per cent of the sale proceeds ranked as set out above. Unsecured creditors are satisfied by the remaining 10 per cent of the sale proceeds.

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## Employment-related liabilities in restructurings

### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Under Greek law an employer can terminate an employment contract of indefinite duration by notifying the employee in writing and paying the statutory compensation. Failure to pay the statutory compensation or notify the employee in writing renders the termination null and void. When a debtor is declared bankrupt contracts are not automatically terminated. The bankruptcy administrator can terminate employment contracts lawfully without paying the statutory compensation at the time the termination occurs. The employee maintains a claim for his compensation.

A restructuring does not automatically exempt a debtor from complying with the collective redundancies restrictions (up to 5 per cent for larger employees) and there is no case law on this point. However, where a business ceases operations as a result of the appointment of a bankruptcy administrator, or when there is a downsizing as a result of a judicially ratified recovery or reorganisation plan, it is arguable that those employee terminations do not count towards the statutory threshold (in the sense that they are the result of closures pursuant to a judicial decision).

Claims for unpaid wages and salaries as well as claims for termination compensation are treated as priority claims in liquidation and are usually satisfied to a substantial extent. The state-run social security fund is also a privileged priority creditor but there is no similar provision for other employee pension funds or schemes.

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## Pension claims

### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Claims by the Social Security Fund dating from 24 months prior to the declaration of insolvency are treated as priority claims and are satisfied as a matter of general priority (set out in greater detail in question 33).

Employee claims that have arisen within two years of the declaration of insolvency are also given special priority under statute. The Bankruptcy Code does not distinguish between claims for unpaid wages and salaries and claims for unpaid voluntary benefits such as unpaid pension contributions, which are also given the same priority.

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## Environmental problems and liabilities

### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

If the environmental problems take place after the commencement of insolvency proceedings, and arise by action of the bankruptcy administrator, the person suffering the damage may file a lawsuit against the bankruptcy administrator, under his or her capacity as administrator of the insolvency estate, and upon acquisition of an enforceable title, he or she may be satisfied before the other creditors by the insolvency estate. If the debt cannot be satisfied by the insolvency estate, the

bankruptcy administrator is obliged to compensate the creditor, if he or she failed by reason of gross negligence to diagnose that the estate is not likely to be able to satisfy such group debt or actually diagnosed it, but neglected it.

Of course, liability of the bankruptcy administrator under tort is not precluded. In any case, any claim against the bankruptcy administrator is time-barred after a period of three years from the time the person suffering the damage became aware of the damage and of the damaging act.

If the environmental problems take place after the commencement of insolvency proceedings by the action of the debtor, the person suffering the damage may file a lawsuit against the debtor and, upon acquisition of an enforceable title, he or she may be satisfied by the debtor's estate. It should be noted that the person suffering the damage may be satisfied by the debtor's property that was acquired after the opening of insolvency proceedings and that is not included within the insolvency estate.

If the environmental problems take place before the commencement of insolvency proceedings, the person suffering the damage must participate in the insolvency proceedings (by announcing its claim) in order to be satisfied by the insolvency estate.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

As stated above, a recovery agreement may provide for liabilities that pass to the new acquirer or purchaser of debtor's assets and for the discharge or conversion of other liabilities. Otherwise, liabilities continue to lie with the debtor. The debtor, if a physical person, is discharged either after the lapse of 10 years as of the declaration of bankruptcy, or if he has repaid all creditors in principal and interest. The debtor, if a legal entity, is discharged if it has repaid all creditors in principal and interest. The discharge of a debtor who was convicted for elimination or non-disclosure of assets belonging to the insolvency estate, for acting in a manner contrary to the rules of prudent financial management and for non-keeping or concealing of mandatory business books, is prohibited, unless criminal discharge for these acts occurred.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Following liquidation of the debtor's estate, the bankruptcy administrator draws up a list with regard to distributions that will be made to creditors. The bankruptcy administrator may proceed in provisional distributions after having obtained the reporting judge's prior consent. The list of distributions is submitted to the latter and it is posted at his office. Public notification at the Bulletin of Judicial Publications of the Jurists' Pension Fund is required as well. Under certain circumstances, the publication of the list of distributions in Greek political and economic daily gazettes or economic gazettes of international circulation may be required.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The debtor's transactions that took place during the interval between cessation of payments and declaration of bankruptcy (suspect period) are annulled or may be annulled.

The following transactions that are restrictively enumerated within the Bankruptcy Code are presumed to prejudice creditors' interests and are automatically null and void:

- donations and gratuitous acts;
- payments of debts that did not fall due and payable;
- payments of due debts that were not made in cash; and
- creation of security over the debtor's estate for pre-existing debts.

Any debtor's mutual transaction may be annulled if the debtor's counterparty did not act in good faith, that is, it knew that the debtor has suspended its payments and that the transaction was detrimental to creditors' interests.

Another ground upon which the debtor's transactions can be annulled, is the fraudulent prejudice of creditors' interests. More specifically, fraudulent acts committed by the debtor during the last five years prior to the declaration of bankruptcy to the detriment of its creditors' interests or to establish a preference of some creditors over the others, can be avoided and the assets are recovered by the debtor, provided that the third party knew of the debtor's intent.

No transaction contemplated pursuant to a ratified reorganisation plan or a recovery agreement can be annulled.

Apart from the Bankruptcy Code, there are additional provisions stipulating acts that are exempted from bankruptcy revocation, including any mortgage or loan granted by a company under the Law of 17.07/13.08.1923 and Law 4001/1959 to secure a loan; any pledge or mortgage granted to secure claims from bond loans issued according to Law 3156/2003; the transfer of claims pursuant to Law 3156/2003 regarding the securitisation of claims; and within the framework of Law 3389/2005 regulating PPPs, any securities granted by an SPV or any third party in favour of a credit or financial institution or any third party in order to secure claims towards the SPV.

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

Yes, Greece has the concept of a suspect period. It is defined as the period between the date on which the debtor actually ceased payments and the date on which it was declared bankrupt. The decision that declares the debtor's bankruptcy will also set the date on which payments are deemed to have ceased. This period may not be longer than two years.

In principle, the annulment of a transaction that occurred during the suspect period is made by the liquidator. Nevertheless, creditors are not deprived of their right to claim the annulment of a transaction provided that the bankruptcy administrator, after being informed in writing, failed to act. Proceedings to annul transactions can be initiated right after a debtor is declared bankrupt irrespective of the bankruptcy proceedings that will follow, leading to reorganisation or liquidation. See also question 38.

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### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Failure to withhold or pay income tax, or to collect or pay VAT by a corporate entity makes the directors, administrators, executive managers, executive directors and bankruptcy administrators of a joint-stock company liable for payment of such tax. Similarly, management members are also liable for payment of income tax owed by the company or withheld by a company that was wound up. Moreover, failure to pay certified tax debts is a criminal offence for which liability attaches to the company management. The management is also criminally liable for the non-payment of salaries and other employment dues (including social security contributions).

If management fails to file promptly a petition for the declaration of bankruptcy, its members may be held personally liable for the satisfaction of additional debts incurred by the debtor from the date the petition should have been filed until the actual declaration of bankruptcy. Furthermore, if bankruptcy is the result of a fraudulent act or gross negligence attributable to any members of management, the responsible persons are liable to compensate creditors.

In addition, criminal sanctions may be imposed on officers and directors in cases of, for example, hiding assets, onerous transactions, disposal of merchandise at an undervalue, false statements and dissipation of debtor assets.

### Update and trends

The deficiencies of the bankruptcy and pre-bankruptcy proceedings generated the need for a general reform of the bankruptcy law. In particular, the lack of qualifications of the bankruptcy administrators, as well as their lack of relevant practical experience, the improper use of provisional measures by some debtors seeking to avoid the payment of their debts, the time-consuming stage of announcement and verification of creditors' claims led to several amendments of particular provisions of the Bankruptcy Code that were introduced by Law No. 4336/2015 that came into force on 14 August 2015. There have been positive steps in rendering the bankruptcy and pre-bankruptcy proceedings more efficient, but it may seem that there are still inefficiencies, which are analysed, below.

Moreover, Law No. 4336/2015 provided for shortening of the time-limits with regard to the verification of creditors' claims. In particular, the deadline for the announcement of claims was amended from three months to one month, starting from the publication of the decision declaring the bankruptcy. The deadline for the verification of creditors' claims was limited to one month rather than the three months provided under the previous law.

Furthermore, the deadline for objections was shortened to 10 days starting from the completion of the verification stage, while the hearing of such objections was determined to be 20 days from their introduction, in place of the previous wording, providing for the submission of objections 'without undue delay'.

Whether the amendments above will actually assist in the acceleration of the administration of bankruptcies will be assessed in practice. It is worth noting that since its entry into force, namely since 10 July 2007, the Bankruptcy Code provides as a general rule that the hearing of cases before the Bankruptcy Court will be set within 20 days from their submission, while the judgment will be issued no further than 15 days from the hearing. However, this provision was never respected in practice because of the heavy workload of the courts. Likewise, it is very possible that the deadline for the hearing of objections before the Bankruptcy Court may not be applied in practice, particularly if one considers the overloaded lists of cases and the multiple adjournments granted in practice.

Restitution is possible only after 10 years from the declaration of bankruptcy, far from allowing a second chance for entrepreneurs. An amendment is necessary in order to provide for full discharge of debts after a much shorter period (not later than three years), but with appropriate restrictions in order to avoid encouragement of dishonest debtors and unfair detriment of creditors' interests. Law No. 4336/2015 (which entered into force from 1 November 2016 for bankruptcies declared after 1 January 2016) provides for discharge three years after a finding by the bankruptcy court that the debtor has not acted in bad faith or with intent; such a hearing usually takes place at the conclusion of the bankruptcy, which usually comes nearly or more than a decade from commencement. Accordingly, this provision is unlikely to lead to a quick fresh start for Greek bankrupts.

The discharge period must be reduced to three years starting from:

- the date of the declaration of bankruptcy, in the event the bankruptcy is concluded either through a liquidation of the debtor's estate or through a closure of bankruptcy procedures; or

- the date of the ratification of the reorganisation plan of article 107 GBC.

The duration of the liquidation procedure described in the GBC may last up to 10 years, resulting in a number of inefficiencies, such as the devaluation of the bankrupt estate, the encumbrance of the judicial systems with long-lasting cases and the accrual of losses to creditors. A more speedy procedure is, therefore, necessary, in order to rectify these inefficiencies and to reduce the costs involved.

Creditors cannot verify that the property revealed by the debtor is actually the total property that the bankrupt debtor possesses. An amendment could be adopted, according to which the applicant debtor has to give his or her consent so that the respective creditors have access to all the debtor's data maintained by all authorities, such as tax authorities, real estate registries, credit institutions (including access to deposit accounts data), in order to verify the debtor's estate. Insofar as the recovery process is concerned, the law provides for an automatic stay of all individual measures against the debtor as soon as the pre-pack is filed; however, such stay may not exceed a four-month period. This amendment may also generate practical deficiencies, if one considers an adjournment of the initially determined hearing date following a petition filed by a creditor who acts in bad faith. Taking into account the fact that the hearings following such an adjournment are usually determined at minimum four to five months later, it can be easily concluded that in that way an effort of recovery may be jeopardised and will not flourish, since any dissenting and non-contracting creditor may initiate individual measures against the debtor's estate.

The GBC establishes the compulsory enforcement (through a court decision) of debt into equity conversion, even without shareholder's consent, if the bankruptcy court decides that any shareholder refuses abusively to grant its consent. Abusive refusal exists when the bankruptcy court decides that without the conclusion of a recovery agreement, the debtor will become insolvent, and the sale proceeds will not suffice for the satisfaction of the shareholders. There is no recorded case law for the implementation of the provision in question.

There are many individuals involved in the different processes provided in GBC. Bankruptcy administrators, experts and mediators play a crucial role in the procedures, either the rehabilitation ones or the liquidation. The job of these people should be assumed by insolvency practitioners, who should have the expertise and training to deal with insolvency matters. The profession of the insolvency practitioner has already been established by Law No. 4336/2015, but it will be in force from 1 October 2016. The issuance of the relative Presidential Decree describing the typical qualifications of the profession is still pending whereas it must be issued the soonest possible.

Although the GBC regulates commercial insolvency and Law No. 3869/2010 consumer insolvency, there are common underlying principles and objectives (both for restructuring and for liquidation procedures) that need alignment. Uniform application of such principles and objectives, subject to necessary variations, is desirable, irrespective of their legal capacities. International legal practice favours compilation of corporate and consumer insolvency.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

As a general rule, the parent company is not liable for the corporate debts incurred by any of its affiliates or vice versa. This is in accordance with the principle of separate corporate personality of each company member of a group. Nevertheless, a parent company or an affiliated corporation may be responsible for the liabilities of a subsidiary or an affiliated company if, under the terms of any concluded agreement, the former is co-debtor or guarantor of the latter.

In a case of joint and several liability, if any of the co-debtors (including the principal debtor) is declared insolvent, the creditor has the right to claim full satisfaction of its claim from each co-debtor if, at the time any co-debtor became insolvent, its claim was actually due and payable. If a creditor enforces its claim against one or more co-debtors and receives an amount exceeding the amount of its claim, then, the creditor must reimburse any co-debtor that has a right of recourse against the principal debtor or any co-debtor.

Similarly, in the case of a company that is a guarantor of another company member of the group, the creditor may exercise its rights

against the principal debtor that is declared insolvent as well as against the guarantor. In the case of excess payment of its claim, the creditor reimburses the guarantor with the excess amount provided that the latter has the right of recourse against the principal debtor. Alternatively, the creditor may reimburse the excess amount to the bankruptcy administrator.

The GBC does not provide for substantive consolidation in case of bankrupt company members of an enterprise group. Hence, the Bankruptcy Court cannot order a distribution of group company assets pro rata without regard to the assets of the individual corporate entities involved.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

The Bankruptcy Code provides a set of rules for the annulment of transactions contemplated during the period from cessation of payments to bankruptcy declaration, and also damage to creditors. The Code presumes that insiders (founders, managers and directors) are

aware of the debtor's suspension of payments, and ordinary arm's-length transactions within the debtor's professional or business activities may not be annulled. Claims against the debtor may be verified by the bankruptcy administrator before the reporting judge against the debtor's books and records. The debtor, the bankruptcy administrator and creditors whose claims have been verified may contest claims asserted against the debtor, in which case the Bankruptcy Court will have the final decision. Finally, the Code provides for criminal sanctions in the event of onerous transactions, disposal of merchandise at an undervalue, false statements, dissipation of debtor assets, false acceptance of debts and favourable treatment of the creditor.

#### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Under Greek law a seizure requires an executory title and a supervised public auction. However, tax authorities are entitled to impose a seizure on debts over €70,000 without obtaining an executory title first. Such significant reform was introduced by Law No. 4336/2015.

#### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Greek laws provide procedures for liquidation or dissolution of all forms of corporations. The general rule is that liquidation or dissolution of a corporation does not affect its ability to be declared bankrupt. Special purpose legal entities such as credit institutions and companies providing investment services can be declared bankrupt, although any bankruptcy proceedings may be suspended if the Bank of Greece orders the winding up of the credit institution or the Hellenic Capital Markets Committee revokes its licence, leading to an initial stage of distribution of segregated client assets (confusingly named 'special liquidation') and, thereafter, to liquidation or bankruptcy. Insurance companies can be declared bankrupt but not prior to the conclusion of a special winding-up process introduced by Legislative Decree 400/1970, as amended by Presidential Decree 332/2003.

#### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Recovery and reorganisation proceedings are concluded upon judicial ratification of the respective plan. Liquidation proceedings are concluded upon liquidation and distribution of all the debtor's assets (article 164). In addition, insolvency will be terminated if: the corporate assets are inadequate to satisfy creditors' claims; or 15 years have elapsed since the formal declaration of bankruptcy.

#### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

EU Regulation 1346/2000, which came into force on 31 May 2002, applies, since Greece is an EU member state. Moreover, Law No. 3858/2010, which came into force on 28 June 2010, substantially repeats the text of the UNCITRAL Model Law on Cross-border Insolvency; caution is required with the definitions, especially that of 'foreign proceedings', as the law seems to apply only to foreign proceedings that involve the appointment of a liquidator. Foreign creditors that seek to commence or participate in bankruptcy proceedings in Greece have the same rights as domestic creditors.

#### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

Each member of a corporate group is subject to distinct bankruptcy proceedings. This is in accordance with the fundamental principle of separate corporate personality of an enterprise group. The Greek Bankruptcy Court does not provide for any procedural consolidation in the case of a bankrupt enterprise group. Nevertheless, it is not precluded for a subsidiary's COMI to coincide with a parent's COMI. In that case, the bankruptcy proceedings will be centralised before the same court. To the best of our knowledge, to date Greek courts have neither addressed any such case, nor rebutted the presumption on the premise that the subsidiary's COMI is actually the parent's COMI.

#### Cross-border cooperation

#### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Law No. 3858/2010, which implemented most of the UNCITRAL Model Law, introduces the prospect of recognition of foreign insolvency proceedings as well as the cooperation among Greek courts, foreign courts and liquidators of different jurisdictions. There are no reported cases in which the court refused to recognise foreign proceedings. On the

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other hand, there are judgments reported in which Greek courts recognised foreign main proceedings and initiated secondary bankruptcy proceedings in Greece according to the provisions of the European Insolvency Regulation.

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**Cross-border insolvency protocols and joint court hearings**

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- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

The Greek courts have not concluded any cross-border insolvency protocol or other arrangement that regulates coordination if concurrent insolvency proceedings are opened within different jurisdictions. However, Law No. 3858/2010, which implemented most of the UNCITRAL Model Law, introduces the prospect of cooperation among the Greek courts, foreign courts and liquidators in different jurisdictions. Because of its relative novelty, that provision has not yet been tested in practice.

# Hong Kong

Georgia Dawson and Look Chan Ho

Freshfields Bruckhaus Deringer

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

#### General insolvency legislation

The legislation principally applicable to insolvency of companies in Hong Kong is the Companies (Winding Up and Miscellaneous Provisions) Ordinance (C(WUMP)O). Further detail is set out in subordinated legislation, the most important of which is contained in the Companies (Winding up) Rules (CWUR), which largely govern the procedural matters in the winding up of a company, and the Companies (Disqualification of Directors) Proceedings Rules.

Certain provisions in the Bankruptcy Ordinance, which governs personal insolvency, may also be relevant to corporate insolvency to the extent that the C(WUMP)O applies those provisions specifically by reference. Other legislation that may be relevant in a corporate insolvency in Hong Kong include:

- the Companies Ordinance (the CO), relating to general company law, including company formation and dissolution;
- the Conveyancing and Property Ordinance (the CPO), relating to voidable disposition of property and the powers of a receiver;
- the Protection of Wages on Insolvency Ordinance (the PWIO) relating to employees' claims for payments from the Hong Kong government's Protection of Wages on Insolvency Fund (the PWIF); and
- the Transfer of Businesses (Protection of Creditors) Ordinance (TBO) relating to the transfer of the business of a company in certain circumstances.

Other legislation may also contribute to the body of insolvency law in Hong Kong. Insurance companies and banks, for example, have specific legislation applicable to their insolvency, which may supplement, modify or disapply certain provisions in the C(WUMP)O governing general corporate insolvency. Case law also plays a significant role in the interpretation of insolvency legislation.

Many of the provisions in the C(WUMP)O and CWUR date back to the insolvency provisions in the English Companies Acts of 1929 and 1948, but Hong Kong did not follow many of the subsequent revisions to the English insolvency regime (such as the administration or company voluntary arrangements procedure). The Hong Kong government recently enacted a new Companies Ordinance, which significantly reformed corporate governance and modernised company law in general. However, the statutory provisions relating to insolvency and winding up were not affected and remain in their pre-existing form (albeit now contained in the C(WUMP)O); the government has announced that it intends to introduce an insolvency reform bill that will provide for, inter alia, the introduction of a provisional supervision regime (analogous to the English administration procedure) and the concept of insolvent trading. However, the timetable for the introduction of such a bill is presently unclear.

The C(WUMP)O is subject to some prospective amendments made by the Companies (Winding Up and Miscellaneous Provisions) (Amendment) Ordinance 2016, which has yet to come into force.

#### Determining whether a debtor is insolvent

'Insolvency' itself is not defined by the C(WUMP)O. Instead, it contains the concept of a company being 'unable to pay its debts'. The main reasons that a company will be deemed unable to pay its debts are:

- if the company has not paid a claim for a sum due to a creditor exceeding HK\$10,000 within three weeks of having been served with a written demand for payment (known as a statutory demand);
- if an execution or judgment against the company is unsatisfied;
- if it is proved to the satisfaction of the court that it is unable to pay its debts, also having regard to contingent and prospective liabilities, as they fall due (see the Insolvency Act in England), meaning the company is cash-flow insolvent; or
- if it is proved to the satisfaction of the court that the value of the company's assets is lower than its liabilities, taking into account contingent and prospective liabilities, meaning that the company is balance-sheet insolvent.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Hong Kong does not have any specialist courts that deal solely with insolvency matters, but such matters are usually dealt with by the Companies Court. The High Court can wind up any company incorporated in Hong Kong (and in some cases, foreign companies – see question 3). Any criminal matters must be dealt with by the relevant criminal court.

Corporate insolvency cases are usually heard by a 'companies judge' (a High Court judge with experience dealing with insolvency matters). Appeals from the High Court may be made in the usual course to the Court of Appeal and thereafter (with leave) to the Court of Final Appeal in Hong Kong.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

As a general rule, a company formed and registered under the C(WUMP)O, the CO (or under earlier Companies Ordinances of 1865 and 1911) may be wound up pursuant to section 169 of the C(WUMP)O and can be subject to all forms of insolvency process (either by the court or voluntarily).

Unregistered companies, which include overseas companies registered under Part XI of the C(WUMP)O, can also be wound up by the court; however, no unregistered company may be wound up voluntarily under the C(WUMP)O (section 327(2)). Overseas companies (which are not registered in Hong Kong) may also be wound up under this section provided they have sufficient connection with the jurisdiction – although this is subject to the discretion of the court.

There are special provisions in the Banking Ordinance and Insurance Companies Ordinance relating to the winding up of authorised institutions and insurance institutions in Hong Kong.

The insolvency of partnerships (other than limited partnerships) is governed by the Partnership Ordinance.

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**Public enterprises**


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**4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?**

There is no special regime applicable to the insolvency of a government-owned enterprise and unregistered companies established by statute may be wound up under Part X of the C(WUMP)O.

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**Protection for large financial institutions**


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**5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?**

Under section 52 of the Banking Ordinance, the Hong Kong Monetary Authority (HKMA), in its capacity as regulator of Hong Kong's banking industry, has wide-ranging powers over authorised institutions that are either insolvent or otherwise unable to meet their obligations. These include the ability to appoint a manager to take charge of the business of the bank, or that part of its business or assets that are within Hong Kong (note that such an appointment cannot be made where a winding-up order has already been made in respect of the same institution by the High Court).

In June 2016, the Hong Kong Legislative Council passed the Financial Institutions (Resolution) Ordinance (the Resolution Ordinance). The Resolution Ordinance provides for a special resolution regime for certain licensed banks, securities and futures companies, insurers and financial market infrastructures in Hong Kong.

The Resolution Ordinance will be brought into effect on a date to be appointed by the secretary for Financial Services and the Treasury pending the Legislative Council's passing of the relevant subsidiary legislation. The Hong Kong government and Hong Kong's primary financial services regulators will maintain close liaison with the industry and relevant stakeholders in the formulation of the regulations, rules and codes of practice that will be applicable to the new resolution regime.

Under the Resolution Ordinance, the HKMA, the Securities and Futures Commission and the Insurance Authority are designated to be the resolution authorities for the banking, securities and futures and insurance sectors, respectively.

A resolution authority may conduct resolvability assessments on financial institutions that are within the scope of the regime with a view to identifying any barriers that could prevent or impede the orderly resolution of the institution so that such barriers are removed.

If an institution becomes non-viable for the purposes of the Resolution Ordinance, the resolution authority may take certain resolution actions, including: imposing a statutory bail-in of creditors (ie, a write-down or conversion into equity of certain liabilities); transferring businesses/assets to a bridge institution; and selling all or part of the institution to a purchaser or transferring it into temporary public ownership.

Resolution authorities will also have additional powers. For example, a resolution authority may apply to the Court of First Instance for a clawback order against officers of a financial institution who are deemed to be responsible for the non-viability of the financial institution. The period covered in a clawback order is three years immediately preceding the date on which the resolution of the financial institution is initiated, but the Court of First Instance is empowered to extend this period by up to an additional three years in certain circumstances.

Until the Resolution Ordinance becomes effective, the provisions of the Banking Ordinance and the powers of the HKMA described above continue to apply to HKMA-authorised institutions.

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**Secured lending and credit (immoveables)**


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**6 What principal types of security are taken on immoveable (real) property?**

The principal type of security granted over immoveable property is the legal mortgage. A legal mortgage is a transfer of the whole of the debtor's legal ownership in the property subject to the security. This is subject to the debtor's right to redeem the legal title upon repayment of the debt (known as the equity of redemption). The appearance of ownership remains with the debtor although the legal mortgage effects an absolute transfer subject to the right of redemption.

An alternative is the equitable mortgage, which differs from the legal mortgage in that it creates a charge on the property but does not

convey any legal estate or interest to the creditor. An equitable mortgage can be created by a written agreement to execute a legal mortgage, by a mortgage of an equitable interest or by a mortgage that fails to comply with the formalities for a legal mortgage.

Another alternative to the legal mortgage is the fixed charge. This involves no transfer of ownership but gives the creditor the right to have the designated property sold and the proceeds applied to discharge the debt. A fixed charge attaches to the property in question immediately on creation (or, if the property is acquired later, after creation but immediately on the debtor acquiring the rights over the property to be charged). The debtor may then only dispose of the property once the debt has been repaid or with the consent of the creditor.

A company must register a mortgage or charge (whether fixed or floating) within one month of the date on which it was created (section 335 of the CO); failure to do so will not only expose the company and every person responsible for the company to criminal liability, but also render the security granted by the charge void against any liquidator and creditor of the company (section 337 of the CO).

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**Secured lending and credit (moveables)**


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**7 What principal types of security are taken on moveable (personal) property?**

The principal security devices relating to moveable property are mortgages and fixed charges (see question 6), floating charges, pledges and liens.

A floating charge does not attach to a specific asset but is created over a class of assets – present or future – and allows the debtor to buy and sell such assets while the charge remains floating. In practice, floating charges are generally created over the whole business and undertaking of a company and therefore cover all present and future assets of that company. It is only on the occurrence of certain events, such as default on the repayment of the debt, that the charge attaches to the secured assets that are at that time owned by the debtor. This is called 'crystallisation'. On crystallisation, the charge acts like a fixed charge in that the debtor is no longer free to sell the assets without repayment of the debt or without the consent of the creditor.

A company must register a mortgage or charge (whether fixed or floating) within one month of the date on which it was created (section 335 of the CO); failure to do so will not only expose the company and every person responsible for the company to criminal liability, but also render the security granted by the charge void against any liquidator and creditor of the company (section 337 of the CO).

A pledge is a form of security that gives the creditor a possessory right to the pledged asset. It is usually created by delivering the asset to the creditor, although symbolic or constructive delivery may be sufficient.

A lien is a possessory right of a creditor to retain possession of a debtor's asset until the debt has been repaid. It can be created by contract or by operation of law. The creditor has no right to deal with the asset and the lien is usually extinguished once the asset is returned to the debtor.

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**Unsecured credit**


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**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

Certain creditors may have the benefit of a lien (by contract or by operation of law) over assets in their possession (see question 7). A landlord or other creditor who has completed the distraint against the company's assets before the commencement of insolvency (ie, the company's assets have been seized and sold) may keep the proceeds (there is, however, no equivalent to the English statutory provisions that would allow a landlord to distraint post-commencement of insolvency for up to six months of unpaid rent). A supplier of goods may protect itself by inserting a clause in the supply contract to the effect that title to the goods supplied will not pass to the buyer until payment has been received (known as a 'retention of title' or ROT clause). The contract can either provide for retention of title until the specific goods supplied by the contract have been paid for or, more usually, until all monies outstanding from the debtor have been paid. The creditor is therefore contractually entitled to the return of its goods.

If the above remedy is not available, then an unsecured creditor would have to commence proceedings against the debtor for recovery of its debt. If there is no substantive defence to the claim, the creditor can apply for summary judgment, which could take up to three months. If the debtor can show that it has a real prospect of successfully defending the claim, it could take much longer. In the meantime, if the creditor has evidence that the debtor is likely to dissipate the assets, it can apply to the court for an order that assets up to the amount claimed (eg, bank accounts) be frozen or prevented from being dealt with or dissipated. Once a judgment has been obtained, then proceedings to enforce the judgment can be commenced. Remedies include sending a court officer to seize the debtor's goods or diverting an income source (eg, bank balances or book debts) directly to a creditor (a third-party debt order, formerly known as a 'garnishee order').

There are no special rules for foreign creditors except that a foreign creditor may sometimes be required to provide security for the debtor's legal costs by making a payment into court (although the requirement to provide security for costs can also apply to non-foreign creditors in certain circumstances).

Unsecured creditors are also able to file winding-up petitions.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

There are two different procedures for the voluntary liquidation of a company: a members' voluntary liquidation (MVL) (which is a solvent liquidation) and a creditors' voluntary liquidation (CVL) (typically an insolvent liquidation).

##### Members' voluntary liquidation

If the directors of the company are able to swear a statutory declaration that the company is solvent, a company can be placed into MVL. The MVL is commenced once a 75 per cent majority of the shareholders has resolved to place the company into liquidation. The MVL commences from that date and the shareholders choose the liquidator. On appointment of the liquidator, the powers of the company directors will cease.

If the liquidator subsequently determines that the company is in fact insolvent, the MVL should be converted into a CVL.

##### Creditors' voluntary liquidation

If the company is insolvent, or the directors are unable to swear a statutory declaration as to solvency, a company can be placed into a CVL. Again, a resolution must be passed by a 75 per cent majority of the members to place the company into liquidation. The CVL commences on the date on which the shareholders pass this resolution. The shareholders will also appoint a liquidator, but until the creditors' meeting referred to below has taken place, the powers of that liquidator will be limited.

The directors must then hold a creditors' meeting on the same day or on the next day, at which the creditors will be given information on the company (a statement of affairs). The creditors may also appoint a liquidator if a resolution is passed by a majority by value of the creditors present and voting. If the shareholders have previously appointed a liquidator, the creditors' choice of liquidator will prevail.

Section 228A of the C(WUMP)O is a 'special procedure' that allows the directors, in limited circumstances, to commence a voluntary winding up (without first holding a meeting of the shareholders of the company) if they have formed the opinion that the company cannot, as a result of its liabilities, continue its business. This procedure may be used in limited circumstances only because the directors would have to declare that the winding up should be commenced under section 228A because it would not be reasonably practicable to proceed under another section of the C(WUMP)O. A creditors' meeting will be held and the winding-up process will, in general, follow that of a CVL.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

If a creditor seeks to place a company into involuntary liquidation (which is usually called compulsory liquidation or winding up by the court) that creditor has to petition the court to have the company wound up. The most likely ground upon which a creditor would successfully

petition the court for a winding-up order is that the company is unable to pay its debts (see question 1).

If the court makes a winding-up order, the winding up is deemed to commence at the time of the presentation of the winding-up petition rather than on the date of the order. Any disposition of the company's property and any transfer of shares made after the commencement of the winding up is, unless the court orders otherwise, void (section 182 of the C(WUMP)O).

Once the winding-up order has been made or a provisional liquidator has been appointed by the court, no action may be started or proceeded against the company without the permission of the court. The directors' powers will also cease on that date. In addition, the business of the company ceases except to the extent necessary for it to be wound up.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

There is currently no corporate reorganisation procedure (such as a company voluntary arrangements or administrations procedure) in Hong Kong.

### Schemes of arrangement under section 669 of the Companies Ordinance

The scheme of arrangement (scheme) legislation under section 669 provides a mechanism to enable a company to enter into a compromise or arrangement with its creditors. This process is commenced by an application to court, by either the company or any creditor (or, where relevant, the liquidator), for an order that a meeting of creditors be summoned. Any proposed compromise or arrangement will become binding on the creditors if it is approved by 75 per cent in value and the majority in number of each class of creditors present and voting, and it is then sanctioned by the court. (A company may also enter into a scheme with its shareholders as part of a reorganisation, though a more detailed consideration of shareholder schemes is outside of the scope of this chapter.)

It is open to creditors to challenge the scheme in court at either the hearing for permission to convene the scheme meetings or the hearing to sanction the scheme. The usual grounds for challenge are that the meetings were improperly constituted, the creditors were not given sufficient information or the scheme is unfair. During the scheme process there is no statutory protection for the company from its creditors.

In terms of schemes of foreign companies, Hong Kong law is similar to English case law where a company is entitled to enter into a scheme if it is capable of being wound up in England and Wales. Case law has clarified the position further, confirming that a company could be wound up in England and Wales if it could be said to have 'sufficient connection' with England and Wales.

The question as to what constitutes 'sufficient connection' is one that is dependent on the facts in each case, eg *Re LDK Solar Co, Ltd (In Provisional Liquidation)* [2015] 1 HKLRD 458, which largely followed the approach taken by the English court.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

As noted above, there is currently no corporate reorganisation procedure in Hong Kong.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

There is no express duty on a company to commence insolvency proceedings at any particular time on the grounds of either cash-flow or balance-sheet insolvency.

In Hong Kong, there are currently no 'wrongful trading' or 'insolvent trading' provisions (similar to those in England or Australia) that would allow the liquidators to bring an action against directors for

trading after a time when they knew, or ought to have concluded, that there was no reasonable prospect of the company avoiding insolvent liquidation. (At present, Hong Kong law provides only for fraudulent trading, ie, carrying on the business of a company with intent to defraud its creditors.) It is expected that the government will introduce legislation to address this issue, although the timetable for such a bill is presently unclear.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

A company can carry on business during a reorganisation. If there is a consensual restructuring process under way, the creditors involved in that process (eg, the bank group or a bondholder committee) may require additional information about the company during the restructuring process and increased access to management. Other creditors (eg, suppliers) may also change their terms of business to give themselves greater protection should the reorganisation fail and the company subsequently go into insolvent liquidation. If no formal insolvency proceedings have commenced, creditors who continue to supply goods and services during the reorganisation process will not be subject to a particular statutory regime. Existing contractual arrangements continue to apply (see question 15 for stay of proceedings during liquidation and reorganisation).

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

##### Liquidations

When a company is placed in compulsory liquidation (and the court order has been made), or when a provisional liquidator has been appointed, no action or proceeding may be started or proceeded with against the company or its property without the permission of the court (section 186 of the C(WUMP)O). Permission will be refused if the proposed action raises issues that could be dealt with more conveniently and less expensively in the liquidation proceedings; however, this will not restrict claims made by secured creditors in respect of secured assets.

When a CVL is commenced there is no automatic moratorium on proceedings against the company. The liquidator or any creditor or member may, however, apply to the court for a stay on any proceedings. In an MVL no automatic moratorium applies.

##### Reorganisations

The vast majority of reorganisations are informal and there is, therefore, no strict procedure governing moratoria or stays of proceedings. Sometimes, it may be possible for the company to agree an informal moratorium with its creditors (commonly known as a standstill) before commencing a reorganisation. Otherwise, the company will be at risk of creditors commencing actions to wind it up, enforce security or seize its assets.

A reorganisation that is implemented by way of a scheme of arrangement lacks a moratorium on creditor actions. A dissenting minority (before it is bound to a scheme that has become effective), is able to petition for the winding up or take other legal action against the company and its property. The company or the supporting creditors may seek the appointment of a provisional liquidator in order to benefit from the statutory stay of proceedings while the terms of the reorganisations are being negotiated and implemented.

The Hong Kong government is considering the proposal for a 'provisional supervision' procedure, which would provide a company corporate rescue procedure that offers a moratorium on creditor actions, during which the company and its creditors may negotiate and

implement a reorganisation. However, the timetable for the introduction of the necessary legislation is presently unclear.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

A liquidator can raise any money required on the security of the assets of the company. Such credit would have priority over ordinary unsecured creditors as an expense of the liquidation but only in respect of the new funds.

However, any new loans will not take priority over pre-existing debt secured by legal or equitable mortgages or a fixed charge unless this is permitted under the terms of the pre-existing secured debt. Any new security granted to secure the credit cannot take priority over pre-existing security unless this permitted under the terms of the pre-existing security.

In an informal restructuring, or a restructuring implemented by way of a scheme of arrangement, the obtaining of credit and the use of assets as security is a matter for agreement between the company and its creditors.

### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Prior to the commencement of a formal insolvency procedure, the normal rules on set-off and netting continue to apply. Contractual set-off could be amended by agreement as part of an informal reorganisation. Theoretically, it would also be possible to amend rights of set-off as part of a formal restructuring (eg, via a scheme of arrangement), but this could only be done if it was 'fair' to the relevant creditors. This may be difficult to achieve as rights of set-off are likely to vary from creditor to creditor.

Insolvency set-off applies where there have been mutual dealings between a creditor and the company. The office holder is required to take an account of what is due from each party to the other in respect of dealings and set off the sums due from one party to the other. Insolvency set-off is mandatory and cannot be contracted out of.

### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

##### Reorganisations

In practice, many reorganisations result from informal negotiations with creditors outside of any formal insolvency or restructuring procedures. As a consequence, the terms of the reorganisation, and therefore any provisions as to the sale or use of assets, are subject to negotiation between all relevant parties.

##### Liquidations

Once a company has gone into liquidation, the directors will be unable to sell its assets. Instead, the liquidator can sell any of the company's property by public auction or private contract, provided the assets are beneficially owned by the company. This power can be exercised by the liquidator in both voluntary and compulsory liquidations without sanction of the court or committee of inspection.

##### 'Stalking horse' bids and credit bidding

There is no specific legislation that either prevents or encourages the use of 'stalking horse' bids in sale procedures. How a particular sale process is carried out will be at the discretion of the directors or liquidator or provisional liquidator (as applicable).

Credit bidding in sales is permitted, although there is also no specific legislation on this point; in considering whether to sanction such an arrangement the court is likely to assess whether accepting the bid is consistent with the liquidator's duty to act in the best interests of the whole body of creditors.

### Intellectual property assets in insolvencies

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

There is no automatic right of a licensor or owner of IP to terminate the debtor's right to use IP assets. Such matters will be governed by the terms of the licence (eg, in particular in the event of default and termination provisions). In addition, an insolvency representative does not have the power to terminate a debtor's agreement with an IP licensor or owner and then continue to use the IP for the benefit of the estate.

### Personal data in insolvencies

- 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Hong Kong provides statutory protection for the personal data of individuals, under the Personal Data (Privacy) Ordinance Cap 486. While there has not been any case law in Hong Kong concerning the status of insolvent companies or the responsibilities of liquidators under the Ordinance, we would expect a Hong Kong court to follow the reasoning of the English High Court in *Re Southern Pacific Personal Loans* [2014] Ch 426. The English court held that the insolvency of a company has a neutral effect on its responsibilities under the equivalent English Data Protection Act 1988 (the DPA). The court also held that liquidators do not constitute data controllers in their own right and are not personally responsible for the company's compliance with the provisions of the DPA. The liquidators instead act as agents for the company in taking decisions on its behalf.

The liquidators in that case were concerned that the insolvent company should not be required to continue to hold personal data in order to comply with data access requests made by former customers. The court agreed that, in principle, personal data should be destroyed as soon as possible after the company ceases to conduct business, provided that the company must retain sufficient data to comply with any outstanding data access requests made before the data is destroyed. The court further qualified the principle by saying that liquidators must ensure that the company retains sufficient data to enable them to deal with any claims that may be made in the liquidation. The court held that in circumstances in which the liquidators had reason to anticipate the possibility of claims, they would be required to advertise for claims against the company and allow sufficient time for responses before disposing of personal data.

Although the *Southern Pacific* case did not deal with the question of the transfer of personal data to a purchaser of the company's assets, it follows that an insolvent company's position with respect to transfers of data would also be unaffected by the insolvency. A Hong Kong company does not have an automatic right to dispose of personal data as part of a sale of its assets. Any transfer of personal data to a third party that is not consistent with the purposes for which the data was originally collected would require the consent of the individual data subjects concerned. On the other hand, a sale of the shares in the insolvent company preserves the status quo (namely that the company remains the data controller) and does not require a separate consent. In practical terms, liquidators proposing to sell the company's assets, including its data, should ensure that consent to the transfer to a purchaser was obtained at the time the personal data was originally collected (which will not invariably be the case).

### Rejection and disclaimer of contracts in reorganisations

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

A liquidator may disclaim any onerous property with the permission of the court (and subject to section 268 of the C(WUMP)O) at any time in the 12 months after the commencement of the winding up. Onerous property is defined as any property consisting of land burdened with onerous covenants, of shares or stock in companies, or unprofitable contracts, and any other property of the company that is unsaleable, is not readily saleable or is such that it may give rise to a liability to pay money or perform any other onerous act. A contract may be unprofitable if it gives rise to prospective liabilities and imposes continuing financial obligations on the company that may be detrimental to the creditors. A contract is not, however, unprofitable merely because it is financially disadvantageous – it is the nature and cause of the disadvantage that will be the decisive factor. The liquidator cannot disclaim a completed contract. This is because if the company has fully performed then it will have no prospective liabilities, which means that the contract is not onerous and therefore cannot be disclaimed.

The liquidator loses his or her right to disclaim if he or she fails to give notice of a disclaimer within 28 days of service of a notice by the other party requiring the liquidator to decide whether to disclaim. The effect of the loss of the right to disclaim is that the liquidator loses the right to terminate the contract unilaterally by notice, thus enabling the other party to elect to hold the contract open for future performance. If the liquidator chooses to allow the company to default on its obligations, the contract continues in force until the other party exercises a right to treat it as repudiated or obtains an order for rescission of the contract.

A disclaimer operates so as to determine, as of the date of the disclaimer, the rights, interests and liabilities of the company, but does not affect the rights or liabilities of any other person except as far as is necessary for the purpose of releasing the company from any liability. Any person suffering loss or damage as a consequence of the operation of the disclaimer is deemed a creditor of the company and may submit proof for the loss or damage in a winding up.

### Arbitration processes in insolvency cases

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

See question 15. Where a winding-up order has been made, no action or proceedings may be continued or commenced against the company or its property, except with the permission of the court. Arbitration of disputes is likely to be treated as a legal process that would be subject to the same stay of proceedings.

### Successful reorganisations

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

There are no mandatory features in an informal reorganisation – it is a matter for agreement between the creditors – and neither are there any mandatory features of a reorganisation plan in a scheme of arrangement. When an insolvent company proposes a scheme, however, it should be compared against the 'liquidation analysis' (ie, the rights that the creditors would have against the company in an insolvent liquidation). The rights of creditors under a scheme can differ from those creditors would have if the company went into insolvent liquidation; indeed, the purpose of many schemes is to produce an arrangement that differs from an insolvent liquidation. Depending on the differences, however, this may have an impact on the analysis of which creditors form

a separate class for the purposes of the scheme meeting and whether the scheme is fair and should be sanctioned. If the differences apply equally to all creditors, no question of separate classes arises. If the differences produce a result that affects one group of creditors differently from another then, subject to questions of materiality, they should form separate classes.

In a scheme, the process is commenced by an application to the court, by either the company or any creditor (or, where relevant, the liquidator or provisional liquidator), for an order that a meeting of creditors be summoned. There are separate creditors' meetings for each class of creditors. It is the responsibility of the party proposing the scheme to determine the correct classes. If incorrect class meetings are held, then the court will not have the jurisdiction to sanction the scheme.

The classic test for determining the constitution of classes is that a class should comprise 'those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest'. Each class is determined in accordance with the creditors' rights under the scheme, as opposed to broader collateral interests, and it should be noted that a broad view should be taken of the meaning of class and whether a group of creditors forms a single class depends on the analysis of:

- the rights that are to be released or varied under the scheme; and
- the new rights (if any) that the scheme gives, by way of compromise or arrangement, to those whose rights are to be released or varied.

It can be seen from this that in many cases it is not possible to be certain that a particular type of claim constitutes a class of creditors. In certain cases, however, the distinction is relatively clear-cut; for example, secured creditors and unsecured creditors will almost certainly constitute separate classes.

In order for any proposed compromise or arrangement put forward under a scheme to become binding on the creditors it must be approved by 75 per cent in value and the majority in number of each class of creditors present and voting, and then sanctioned by the court. The scheme will not be sanctioned unless it is fair – that is, a scheme that an intelligent and honest person, a member of the class concerned, and acting in his or her best interests might reasonably approve.

The English court has confirmed (see *La Seda de Barcelona SA* [2010] EWHC 1364 (Ch)) that, in the case of an English scheme of arrangement, guarantors that are themselves not bound by the scheme of arrangement can have their guarantees released under the terms of the scheme. The court was particularly influenced by the fact that in return for gaining the benefit of those releases, the guarantor company was itself releasing various group companies from outstanding inter-company debt obligations. This element of 'give and take' was seen as important in establishing a benefit to the scheme creditors, and satisfying the court that its sanction of such releases would be appropriate. This decision is likely to be highly persuasive in Hong Kong.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

Many reorganisations result from informal negotiations with creditors outside any formal insolvency or restructuring procedures. As a consequence, the terms of the reorganisation and, therefore, any provisions as to the timetable for the reorganisation are subject to negotiation between all relevant parties.

There are no provisions for the expedition of schemes of arrangement, and the implementation time for a scheme will depend on its complexity, although the majority of the time spent on the reorganisation is in negotiation with the creditors and in preparation of the settlement documentation. The court has been willing to hear applications on an expedited basis where there is an urgent requirement to do so.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A proposed scheme of arrangement can be defeated if it does not obtain the statutory majorities of creditors voting in favour of it. Assuming that the requisite majorities vote in favour at the scheme meeting, a scheme will be defeated if the court refuses to sanction the scheme either

because it does not have the jurisdiction to sanction it, for example, because the classes are incorrectly constituted or because it is unfair.

A dissenting creditor can defeat an informal reorganisation by refusing to take part or, where appropriate, by applying for the company to be wound up (although the court has to exercise its discretion when making a winding-up order).

If a scheme of an insolvent company is defeated, then unless new reorganisation proposals can be agreed with the requisite majorities of creditors, it is likely that the company will be placed in liquidation.

If there is default by the debtor in performing an approved plan in a scheme, the consequences of default will usually be set out in the scheme document. The consequences of a breach by the debtor of any informal agreement will depend on the terms of the agreement but will usually result in the creditor having all its previous rights restored.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

##### Notice and meetings

Generally, the C(WUMP)O provides for early notification of all creditors by advertisement and for the holding of a meeting of creditors.

The first creditors' meeting held in a CVL will take place on the same day or the day after the shareholders pass a resolution to place the company in liquidation. At this meeting, the main purposes will be to appoint a liquidator, fix the liquidator's remuneration and potentially appoint a committee of inspection. The liquidator must call a further meeting of the creditors generally if the liquidation lasts more than one year. Before the company is finally dissolved, the liquidator must call a final meeting of creditors.

In a compulsory liquidation, the official receiver is usually automatically appointed as the provisional liquidator until a meeting of the company's creditors and contributories is convened and the court has ordered the appointment of a liquidator. The liquidator must advertise his or her appointment.

In a liquidation (whether it is a CVL or compulsory liquidation), if one-tenth in value of the company's creditors (or contributories) request the liquidator to hold a meeting of creditors, then there is an obligation to do so.

##### Proceedings against third parties

As a general rule, the ability to bring proceedings against third parties in relation to losses suffered by the company is limited to the liquidator or provisional liquidator. One exception when the company is in liquidation is the right of any creditor under section 276 of the C(WUMP)O to bring proceedings against any officer of the company or anyone involved in the formation or promotion of the company in connection with any alleged misfeasance or breach of fiduciary duty. Another exception is where a creditor may commence proceedings for fraudulent trading under section 275 of the C(WUMP)O.

##### Release of third parties

See question 23. It is highly likely that the court has jurisdiction to release guarantee claims against third party guarantors as part of a scheme of arrangement.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Creditors may determine that it is in their best interests to fund the estate or insolvency office holder in order that a claim may be pursued by the insolvency office holder; however, creditors are not themselves able to pursue remedies on behalf of the estate (this being the function of the insolvency office holder) except in the circumstances described in question 26.

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**Creditor representation**

- 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

A committee of inspection may be appointed in a liquidation. The committee may ordinarily consist of no more than five persons.

If a committee of inspection is appointed in either a CVL or a compulsory liquidation its role is mainly supervisory. It also fixes the liquidator's remuneration and has the ability to sanction the exercise of certain of the liquidator's powers (which can also be sanctioned by the court). The liquidator has to report to the committee of inspection on a regular basis.

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**Insolvency of corporate groups**

- 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

Hong Kong law treats each member of a corporate group as an entirely distinct entity from its members, other than in very specific circumstances. Accordingly, the assets and liabilities of companies are not combined into one pool for distribution in an insolvency process. As a practical matter, where there is a corporate group, there may be administrative advantages to having the same insolvency office holder appointed in respect of each of the companies in the group (subject to any conflicts), but each entity will still be treated separately.

Assets would only properly transfer to an insolvency in another country in the event that it was demonstrated to the satisfaction of the relevant insolvency office holder that the Hong Kong company did not have right and title to the asset and that it should in fact be treated as an asset of another company (potentially within the same group). Given the insolvency office holder's duty to ensure the best return to creditors, they would not consent to the transfer of such assets without incontrovertible evidence that this was the case or there was a sale of the assets for value.

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**Appeals**

- 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

In relation to the right of appeal, see question 2. There is no mandatory requirement to post security to proceed with an appeal.

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**Claims**

- 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

Generally, unsecured creditors' claims are not submitted until the company is in liquidation. All creditors submit a claim by sending particulars of it to the liquidator by way of a 'proof of debt'. A creditor may make a claim in respect of a contingent or unliquidated amount provided that it arises prior to the date on which the company went into liquidation (this element has been the subject of much case law).

Time limits may be set for receipt and processing of claims before interim dividends are paid. If the creditor misses the deadline it will be entitled to receive previous interim dividends once it has proved its claim. Once the liquidator has realised all the company's assets he or she will give notice of intention to declare a final dividend. All claims have to be established by the date set out in the notice declaring the final dividend.

The liquidator may reject a proof in whole or in part but must provide reasons to the creditors. A creditor may appeal to the court against a rejection within 21 days of receiving notice of it.

There are no specific provisions dealing with the purchase, sale or transfer of claims against the debtor.

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**Modifying creditors' rights**

- 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

The court does not have general jurisdiction to change the priority of creditors' claims, which are determined by statute; however, where realisations are made from assets subject to a floating charge, and there are insufficient assets to meet the statutory preferential debts, an insolvency office holder must apply the realisations to pay such preferential debts ahead of the floating charge holder.

Rule 179 of the CWUR sets out a list of winding-up expenses and the priority in which they should be paid out of the assets. Pursuant to section 220 of the C(WUMP)O, the court may, in the event of the assets being insufficient to satisfy the liabilities, make an order as to the payment, out of the assets, of the expenses incurred in the winding up in such order of priority as the court thinks just. However, the power of the court only extends to being able to vary the order of priority of the winding-up expenses set out in the aforementioned list. The court does not have jurisdiction to treat costs that are not contained in that list as expenses of the winding up.

The 'anti-deprivation' rule under common law also makes it clear that parties cannot contract out of the statutory rules for the realisation and distribution of assets in insolvency that are contained in the C(WUMP)O.

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**Priority claims**

- 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

An office holder will apply the proceeds of the realised assets and pay creditors in a specified order depending upon the source of the proceeds, that is, whether they come from fixed-charge realisations, floating-charge realisations or the realisations of uncharged assets.

Other than the costs of preserving and realising the fixed-charge assets (including the office holder's costs relating to those assets), there are no priority claims that rank ahead of secured creditors with a fixed charge in relation to the proceeds of the sale of those assets.

In addition to the costs of preserving and realising the floating-charge assets, certain priority claims rank ahead of floating charge holders and these are paid out of the proceeds of sale of the assets secured by the floating charge. These priority claims are preferential debts. Primarily, these include wages and certain government debts.

The costs and expenses of the liquidator rank ahead of payments to unsecured creditors out of the realisation of uncharged assets.

Creditors who can establish valid retention of title and other proprietary claims will have their property returned (or its monetary equivalent) in priority to those listed above. Where there have been mutual dealings between a creditor and the company, the liquidator is required to take an account of what is due from each party to the other in respect of dealings and set off the sums due from one party to the other.

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**Employment-related liabilities in restructurings**

- 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

Contracts of employment will automatically terminate upon a compulsory liquidation. Generally, employees will be unsecured creditors in the liquidation of the company, except to the extent that any of their claims constitute preferential debts under section 265 of the C(WUMP)O (such as unpaid wages and certain employment-related claims up to a limit), which will be paid ahead of other unsecured creditors' claims. Contracts of employment will not automatically terminate upon a CVL as the business of the company does not terminate instantly. This noted, a liquidator only has the 'power to carry on the business of the company so far as may be necessary for its beneficial

winding up'. It is therefore likely that the business of the company will cease shortly after entry into liquidation and at this time the liquidator will terminate any ongoing contracts of employment.

When a liquidator sells part or all of a business in a CVL or MVL he or she must have regard to the TBO, as the transferee may become liable for the debts of the transferor (including employment claims). There are, however, certain exceptions under the TBO that apply to a business that is sold by a liquidator appointed in a compulsory winding up or a receiver pursuant to a charge that has been registered for at least one year.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Certain limited contributions into occupational retirement schemes and mandatory provident fund (under the Mandatory Provident Fund Schemes Ordinance) are categorised as preferential debts under section 265 of the C(WUMP)O.

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

There is no legislation in Hong Kong governing the treatment of such liabilities, thus it is likely that in an insolvency context any environmental liabilities that pre-date the insolvency would be categorised as unsecured claims. It is unclear how any environmental liabilities arising as a result of anything done or omitted to be done by the insolvency office holder would be treated.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Where a debtor uses a scheme of arrangement to reorganise, the terms of the scheme will determine the treatment of the debtor's liabilities (eg, the extent to which they are compromised).

Where a purchaser buys the assets from an insolvent debtor, the liabilities remain with the debtor, apart from certain employment liabilities that may transfer to the purchaser in accordance with the TBO.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In liquidations, a distribution will be made when sufficient funds are available to justify it. In the case of a reorganisation, the terms of any distribution will usually be set out in the restructuring agreement or the scheme of arrangement, as appropriate.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

A transaction may be set aside by a liquidator under the C(WUMP)O if it is an unfair preference. A company grants a preference where it does something, or allows something to be done, that puts a creditor, surety or guarantor in a better position than it would otherwise have been if the company went into insolvent liquidation. The court will, however, only make an order restoring the position to what it would have been if the company was influenced by a desire to put that other person in that better position. This desire to prefer is assumed where the parties are 'associates' (as defined in section 51B of the BO).

'Transactions at an undervalue' as the concept exists in English law are currently not recognised under the insolvency legislation in Hong Kong. However, this concept has been introduced by the Companies

(Winding Up and Miscellaneous Provisions) (Amendment) Ordinance 2016, which has yet to come into force.

In addition to unfair preferences, certain floating charges will also be invalid under section 267 of the C(WUMP)O, except to the extent of any valuable consideration (being money, goods or services supplied, or a discharge or reduction of any debt or interest).

The court will not make any order unless, at the time of making the preference or granting the floating charge, the company was unable to pay its debts, or became unable to pay its debts as a consequence of the transaction.

Separately, a liquidator may apply to the court to set aside an extortionate credit transaction, referring to a transaction including terms requiring grossly exorbitant payments to be made in respect of the provision of credit or otherwise grossly contravened ordinary principles of fair dealing (section 246B of the C(WUMP)O).

A transaction may also be set aside by the court if it is a fraudulent conveyance under section 60 of the CPO, which is a disposition of property made with intent to defraud creditors.

Under Hong Kong law, there are no specific legislative provisions that allow for transactions to be annulled as a result of a reorganisation.

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The 'suspect period' for an unfair preference given to an 'associate' is the two years prior to commencement of the winding up. With respect to a preference given to any other persons, the suspect period is six months prior to the commencement of the winding up.

The suspect period for the avoidance of floating charges is 12 months prior to the commencement of the winding up, and three years prior to the commencement of the winding up for an extortionate credit transaction.

The types of transactions outlined above (other than fraudulent conveyancing under section 60 of the CPO) can only be challenged in a liquidation, and not in any other form of restructuring, and the challenge can only be made by the liquidator.

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### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The company's officers and directors will not generally be personally liable for obligations of their corporations unless they have entered into personal guarantees of those obligations. However, the company's officers can be held to be personally liable to contribute to the assets of the company for any one of the following reasons:

- misfeasance or breach of any fiduciary or other duty (section 276 of the C(WUMP)O); or
- fraudulent trading: section 275 of the C(WUMP)O, which provides that where it appears that any business of the company has been carried on with intent to defraud creditors or for any fraudulent purpose, the court may declare (on application of a liquidator or any creditor or contributory of the company) that any persons who were knowingly parties to the carrying on of business in that manner are personally responsible. This section is not limited to directors and officers but applies to anyone who has been involved in carrying on the business of the company in a fraudulent manner. It is necessary to prove actual dishonesty.

The remedies against some of the above claims that may be brought against the directors are designed to be compensatory for the liabilities incurred by the company.

The company's officers can also be criminally liable under sections 271 to 277 of the C(WUMP)O for fraud, misconduct, falsification of the company's books, material omissions from statements and false representations. They are also liable to disqualification from

being a director of any company for up to 15 years under Part IVA of the C(WUMP)O.

The directors of a company owe a duty to act in the best interests of the creditors (as opposed to those of the shareholders) of the company in the 'twilight period' (ie, when a company is insolvent or on the brink of insolvency (see the English case of *West Mercia Safetyware Ltd v Dodd* [1988] BCLC 250)).

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Generally, Hong Kong law treats each member of a corporate group as an entirely distinct entity from other members of the group, other than in very specific circumstances. Accordingly, a parent or affiliated corporation is not responsible for the liabilities of subsidiaries or affiliates in an insolvency process.

A parent company may conceivably be held liable for the acts of its subsidiary pursuant to the law of agency; however, there is no presumption that a subsidiary is the agent or alter ego of the parent company. In very limited circumstances the Hong Kong courts will permit the piercing of the corporate veil to allow action to be taken against those who control a company.

A parent company may also be liable for the acts of its subsidiaries under the torts of conspiracy and negligence. In particular, depending on the facts, there can be a primary, direct duty of care on a parent company towards employees (and potentially others) affected by the activities of a subsidiary under the tort of negligence.

There is no mechanism under Hong Kong law by which assets may be dealt with at the level of the corporate group without regard to the insolvencies of individual entities.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There are no equitable subordination rules as such in Hong Kong insolvency law. The rules for distribution of an insolvent estate are set out in the C(WUMP)O and CWUR, and shareholders are last in the order of distribution in respect of their share capital, after unsecured creditors have been satisfied in full. Non-arm's length creditors will rank *pari passu* with the remainder of the unsecured creditors unless they have security, in which case the usual rules of distribution will apply.

The rules relating to unfair preference are more stringent if the transaction is with an 'associate' (discussed more fully in question 39). For example, an 'associate' is presumed to be influenced by the desire in giving a preference and the time limit is extended from six months prior to the commencement of the winding up to two years prior.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

A secured creditor can potentially enforce its security outside of court proceedings either by the appointment of a receiver over specified charged assets. The receiver will collect and realise the charged assets towards satisfying the debt. The primary duty of the receiver is owed to the secured creditor (but the receiver acts as the chargor's agent in relation to the charged assets). A mortgagee may take physical possession of the assets subject to the mortgagor's equity of redemption, and such possession does not require a court order. If the mortgagee wishes to foreclose (ie, to become the owner of the assets free of the mortgagor's equity of redemption), an order of the court is required.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

In addition to an MVL, a company may be dissolved under section 750 of the CO without the need for a formal liquidation procedure if all the shareholders agree, the company has never commenced business or

operations or ceased carrying on business or operations longer than three months ago, and the company has no outstanding liabilities.

Pursuant to section 760, such companies, as well as companies that have been dissolved following liquidation, may also be restored to the Companies Register following an application to the court by an interested party within 20 years of the date of dissolution.

The court will make an order for restoration if, at the time of the striking off, the company was carrying on business or in operation or if the court considers it just to do so.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

In the case of a voluntary winding up, once the company's affairs are fully wound up the liquidator must present the final accounts, showing how the liquidation has been conducted, to a meeting of creditors. After the meeting, the liquidator will send a copy of the account to the registrar of companies. The company is then deemed dissolved after three months.

In the event of a compulsory liquidation, if the liquidator is not the official receiver, once the winding up of the company is complete (for practical purposes), the liquidator must summon a final general meeting of creditors. The liquidator will present his or her report of the winding up to the creditors. The liquidator must then notify the registrar of companies that the final meeting of creditors has been held. The company is deemed dissolved three months after the registrar of companies registers this notice. If the liquidator is the official receiver, the liquidation will end three months after the official receiver notifies the registrar of companies that the winding up is complete. Alternatively, if the company has insufficient assets to cover the costs of the liquidation and it appears to the official receiver that the affairs of the company do not require any further investigation the official receiver may apply to the registrar of companies for early dissolution of the company in liquidation.

Schemes of arrangement and informal reconstructions, if successful, will end in accordance with their terms.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

##### Recognition

Under the common law principle of judicial comity, a Hong Kong court will ordinarily recognise a liquidator appointed in the country of the company's incorporation where there are no public policy issues that would prevent recognition (see *Joint Official Liquidators of A Co v B* [2014] 4 HKLRD 374). In addition, it is possible that a Hong Kong court will recognise an insolvency office holder appointed in a jurisdiction other than the company's place of incorporation – though this point has yet to be formally decided.

Hong Kong proceedings may be required to establish the foreign insolvency officer's authority to deal with assets in Hong Kong. Recognition of a foreign insolvency officer's position will, in itself, confer standing on the officer to represent the foreign company in the Hong Kong courts. The officer may bring proceedings in the Hong Kong courts in the name of the foreign company and, generally, administer the assets of the foreign company present in Hong Kong. However, the Hong Kong courts' power to assist a foreign officeholder is limited by the extent to which the type of order sought is available under the Hong Kong insolvency regime and common law or equitable principles: hence the court has recently refused to grant the application of administrators appointed in England and Wales for an order restraining the sale of property subject to a fixed charge, on the basis that no such statutory moratorium or equivalent power exists in Hong Kong (see *Joint Administrators of African Minerals Ltd (in administration)*

*v Madison Pacific Trust Ltd & Shandong Steel Hong Kong Zengli Ltd* [2015] HKEC 608).

### Foreign creditors

In general, foreign creditors and domestic creditors are treated the same under the Hong Kong insolvency regime. Foreign creditors will be able to provide evidence of their claims in a Hong Kong winding-up proceeding in the normal way. However, if there is a concurrent liquidation of the same company in the foreign jurisdiction, then a creditor proving its claim in Hong Kong will only be entitled to share in any distribution once any amount received in the foreign proceedings has been taken into account. Foreign currency debts are converted into Hong Kong dollars as at the date of the winding-up order. Section 34(3B) of the BO provides that, in the context of personal insolvency, foreign currency debts are to be converted into Hong Kong dollars at the midpoint between the selling and buying telegraphic transfer rates of exchange quoted by The Hong Kong Association of Banks on the day the bankruptcy order is made. There is no equivalent provision in the C(WUMP)O; however, section 264 of the C(WUMP)O provides that the same rules shall apply with regard to the respective rights of secured and unsecured creditors and to debts provable in a winding up as apply to the same in bankruptcy. The High Court has held that, in relation to foreign currency debts provable in a winding up, this means that the relevant date is that of the making of the winding-up order rather than the presentation of the petition (see *Re Moulin Global Eyecare Trading Ltd* [2007] HKCFI 747).

### Recognition of judgments

Generally, Hong Kong courts will recognise judgments and orders made by courts in another jurisdiction where the Hong Kong courts consider that such judgment or order has been properly made under that foreign law and that the foreign court had the necessary jurisdiction. The court will normally try to act in a way consistent with the orders of courts of other competent jurisdictions, but this does not justify a departure from the normal rules of conflict of laws whether in the insolvency context or more generally. Although the Hong Kong courts have not formally adopted the approach of the UK Supreme Court in the recent case of *Rubin v Eurofinance SA* [2012] UKSC 46, judicial reaction to the decision has generally been favourable. There may be circumstances, however, where the Hong Kong court will restrict the application of a foreign insolvency order to protect Hong Kong creditors. Therefore, if there are concurrent liquidations, one of which is in Hong Kong, the Hong Kong courts may refuse to hand over Hong Kong assets to the foreign office holder (even where there is a foreign order to that effect), where to do so would prejudice the rights of creditors who have proved their claims in the Hong Kong liquidation.

### UNCITRAL Model Law

Hong Kong has not implemented the UNCITRAL Model Law on Cross-Border Insolvency, which would have provided to a foreign insolvency representative a menu of cross-border insolvency regimes to consider when seeking judicial assistance, including the ability of a foreign

insolvency representative to apply for insolvency proceedings in Hong Kong, to participate in insolvency proceedings already commenced, and to seek recognition and relief for foreign insolvency proceedings.

Hong Kong has entered into reciprocal enforcement treaties with a number of foreign jurisdictions. Hong Kong and China have a memorandum of understanding in place that would give mutual recognition of certain types of judgments.

### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

A company's COMI is a concept derived from the EC Insolvency Regulation (EC) No 1346/2000 in the context of the EU and the UNCITRAL Model Law on Cross Border Insolvency for those countries which have adopted the Model Law. As Hong Kong is neither a member of the European Union, nor has adopted the Model Law, the concept of COMI is of limited relevance under Hong Kong law. As discussed above (see questions 3 and 13), when deciding whether to exercise jurisdiction over a company, it is more likely that a Hong Kong court will have regard to the sufficient connection test.

### Cross-border cooperation

#### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Yes, provided certain standing requirements are met – see further in question 47.

### Cross-border insolvency protocols and joint court hearings

#### 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

Insolvency protocols have been used in cross-border insolvencies between insolvency representatives appointed by the Hong Kong court and the insolvency representatives in a number of other jurisdictions (eg, Bermuda and the Cayman Islands) to harmonise proceedings between the two relevant countries.

In the *Lehman Brothers* case, it was clear that, due to the volume and size of the claims involved and the international dimension of the business, international cooperation would be of paramount importance. In



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2009, Lehman Brothers insolvency representatives in several jurisdictions, including Hong Kong, signed a protocol that focused on cooperation and exchange of information. The Hong Kong courts had in the past approved Hong Kong insolvency practitioners entering into and implementing such protocols in similar cross-border insolvency cases; in general, the court will proceed on the (rebuttable) presumption that the liquidator will normally be in the best position to take an informed and objective view as to what is in the best interests of the liquidation.

# Hungary

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The main provisions concerning the insolvency of an economic operator are regulated in:

- Act XLIX of 1991 on Bankruptcy Proceedings and Liquidation Proceedings (the Bankruptcy Act);
- Act CXXXII of 1997 on Hungarian Branch Offices and Commercial Representative Offices of Foreign-Registered Companies;
- Act LXXXVIII of 2014 on Insurance Business Activity;
- Act I of 2012 on the Labour Code;
- Act V of 2013 on the Civil Code;
- Act III of 1952 on the Code of Civil Procedure;
- Act XXXVII of 2014 on the Further Development of the Institutional System Promoting the Security of Certain Actors of the Financial Intermediary System; and
- 106/1995 (IX.8.) Government Decree on the Requirements of Environmental and Nature Protection during Liquidation and Bankruptcy Proceedings.

The court shall declare the debtor insolvent:

- upon the debtors failure to settle or contest his previously uncontested and acknowledged contractual debts within 20 days of the due date, and failure to satisfy such debt upon receipt of the creditors written payment notice;
- upon the debtors failure to settle his debt within the deadline specified in a final court decision or order for payment;
- if the enforcement procedure against the debtor was unsuccessful;
- if the debtor did not fulfil his payment obligation as stipulated in the composition agreement concluded in bankruptcy or liquidation proceedings;
- if it has declared the previous bankruptcy proceedings terminated; or
- if the debtor liabilities in proceedings initiated by the debtor or by the receiver exceed the debtor's assets, or the debtor was unable and presumably will not be able to settle its debts on the date when they are due, and in proceedings opened by the receiver, the members (shareholders) of the debtor economic operator fail to provide a statement of commitment – following due notice – to guarantee the funds necessary to cover such debts when due.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Bankruptcy and liquidation proceedings are non-contentious proceedings conducted exclusively by the general court of competence and jurisdiction by reference to the debtors registered office of record on the day when the request for opening the proceedings has been submitted and by the Budapest Metropolitan Court. The Budapest Metropolitan Court shall have exclusive jurisdiction to conduct main and territorial insolvency proceedings under Council Regulation 1346/2000/EC on insolvency proceedings concerning economic operators established in a place other than Hungary. Under Hungarian law, no restrictions apply to matters the courts may deal with.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The Bankruptcy Act shall apply to all economic operators such as business associations, private pension funds, associations and their creditors.

All assets held by the economic operator in bankruptcy or under liquidation proceedings at the time of the opening of proceedings, as well as all assets acquired during the proceedings shall be realised in bankruptcy and during liquidation proceedings. The assets of an economic operator shall comprise all assets that it owns or controls.

Assets such as natural preservation areas, land reserved for compensation purposes and taxes and other similar dues taken out of the wages of employees shall not be construed to comprise the economic operator's assets.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The provisions of the Bankruptcy Act apply to government-owned enterprises too. The creditors of a government-owned enterprise have the same remedies as the creditors of a private enterprise.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

In order to maintain the stability of the financial sector the Hungarian parliament adopted the Act XXXVII of 2014 on the further development of the institutional system promoting the security of certain actors of the financial intermediary system, which introduced the resolution system based on the Bank Recovery and Resolution Directive of the European Union. Furthermore the Bankruptcy Act also contains provisions regarding major economic operators. The government may grant this status to economic operators if the settlement of the debts of such operators, composition with creditors or reorganisation are in the interests of the national economy.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

The main types of security on immovables are the real property mortgage and the seceded lien.

A real property may be charged as a security only in the form of a mortgage. The mortgage agreement is valid only if concluded in writing and in the form required for registration in the Land Register and goes into effect when it is registered. Priority is determined according to the date of registration; if more than one request is submitted on the same day, the priority is determined according to the date on which the mortgage agreement was concluded.

The new Civil Code abolished the independent lien. Now, a lien may only be created in connection with a secured claim. However, by introducing the legal institution of 'seceded lien', the new Civil Code has made possible that once a lien (mortgage) has been created, it may be separated from the original claim: the creditor may transfer it without its secured claim, by a written agreement as a security, to its own creditor.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The main types of security on moveables are mortgage on moveables, pledge on moveables, floating charge and security deposit in the form of money or securities.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Unsecured creditors may choose bankruptcy and liquidation proceedings too, however, in this case the rank of their claims will be lower than the rank of the secured ones. Judicial enforcement is another option to choose. Judicial enforcement shall be ordered by the issue of an enforcement order such as certificate of enforcement issued by the court or a notary public, document with an enforcement clause issued by the court or a notary public or a judicial order or restraint of enforcement. Enforcement shall be suspended in case a liquidation process is commenced against the debtor.

No special provisions exist regarding foreign creditors, except that they might be obliged to provide deposit – with the exception of the EU members – to cover the costs of the court process and the appointment of a delivery agent is necessary.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Debtors may request the opening of liquidation proceedings if unable or unwilling to enter into bankruptcy. The petition may be submitted in possession of the prior consent of the supreme body of the debtor economic operator exercising founders' (shareholders') rights. In the case of sole proprietorships, the petition may be submitted by the owner at his own discretion. Employees and the trade unions defined in the Labour Code or the competent works councils shall be duly informed when the petition is filed. Legal representation is mandatory. Commencing a voluntary liquidation has the same effect as commencing liquidation by the creditors.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

If the liquidation is requested by the creditor, the petition to the competent court shall specify the debtor's liabilities, the maturity and a summary of the reasons for claiming that the debtor is deemed insolvent. The documents in proof of the contents of the petition shall also be attached, including a copy of the written notice sent to the debtor. If the court has not rejected the petition it shall notify the debtor by sending a copy of the petition.

Upon the request of creditor the court shall appoint a temporary administrator without delay if the requesting creditor evidences that satisfaction of its claim at a later date is in jeopardy, proves the contract underlying the extent and expiry of the claim, with full probative document, and has advanced the fee of the temporary administrator (200,000 forints if the debtor has no legal personality and 400,000 forints for legal persons) and deposited it at the time of lodging the request.

Commencing a voluntary liquidation has the effect that upon the ruling ordering liquidation of a debtor becoming final, the court shall without delay appoint the liquidator and shall order to have the abstract

of the ruling ordering liquidation and the ruling on the appointment of the liquidator published in the company gazette.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The directors of debtor economic operators may file for bankruptcy at the competent court. Legal representation for the debtor shall be mandatory. The debtor may not file a petition for bankruptcy if already adjudicated in bankruptcy, or if a request for its liquidation has been submitted, and a decision has already been adopted in the first instance for the debtor's liquidation. The debtor may not file another petition for bankruptcy before the satisfaction of any creditor's claim that existed at the time of ordering the previous bankruptcy proceedings or that was established by such proceedings, and inside a period of two years following the time of publication of the final and definitive conclusion of the previous bankruptcy proceedings, or if the court ex officio refused the debtor's request for the previous bankruptcy proceedings pursuant to the provisions of the Bankruptcy Act, and if inside the one-year period following the time of publication of the final ruling thereof.

The petition may be submitted in possession of the prior consent of the supreme body of the debtor economic operator exercising founders (shareholders) rights. In the case of sole proprietorships, the petition may be submitted by the owner at his own discretion. Employees and the trade unions defined in the Labour Code or the competent works councils shall be duly informed when the petition is filed.

If the court did not refuse the request for the opening of bankruptcy proceedings, it shall provide for the opening of bankruptcy proceedings, and shall consequently provide for having the ruling thereof published in the company gazette and for having the indication 'cs. a.' entered in the register of companies next to the company's name. The court shall ex officio appoint an administrator from the register of liquidators in its ruling on the bankruptcy proceedings. The ruling may not be appealed.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Under Hungarian law creditors cannot commence the debtor's reorganisation.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Liquidation proceedings shall be conducted in the event of insolvency of the debtor:

- if no composition is arranged, or if the arrangement fails to comply with the relevant regulations, the court shall dismiss the bankruptcy proceedings and shall consequently declare the debtor insolvent ex officio and shall order the liquidation of the debtor;
- upon request of the receiver;
- upon receipt of notice from the court of registry, if the court of registry has ordered the liquidation of the company; or
- upon receipt of notice from a criminal court.

Any creditor or the liquidator may bring action during the liquidation proceedings for the court to establish that the former executives of the economic operator failed to properly represent the interests of creditors in the span of three years prior to the opening of liquidation proceedings.

Criminal liability of the directors may arise if a company carries on business while insolvent.

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**Doing business in reorganisations**

- 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

In case of reorganisation, the debtor is granted a stay of payment period (moratorium) to preserve the assets under bankruptcy protection, during which the debtor, the administrator, the financial institutions carrying their accounts and creditors are liable to refrain from taking any measure contradictory to the objective of the stay of payment. The stay of payment shall not apply to claims like claims for wages and other similar benefits, claims to any value added tax or to refunds of sums transferred to the debtor's account by mistake.

No special treatment is given to creditors doing business after filing. The directors of a debtor economic operator, including its supreme body and owners, shall exercise their respective rights only if it does not violate the powers vested in the administrator.

The administrator shall approve and endorse any financial commitment of the debtor after the time of the opening of bankruptcy proceedings. The administrator shall have powers to approve any new commitment made by the debtor. However, the administrator may grant approval for a commitment, or for a payment, if they serve the debtors interest in terms of operations, and for the preparation of composition arrangements, and may provide guarantees for such commitments only if agreed by the creditors representing the majority of the claims held by creditors with voting rights.

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**Stays of proceedings and moratoria**

- 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

Under the duration of the stay of payment as a general rule set-off may not be applied against the debtor, payment orders may not be satisfied from the debtors accounts, the enforcement of money claims against the debtor shall be suspended, and the enforcement of such claims may not be ordered, no satisfaction may be sought on the basis of a lien on the debtors assets, the debtor cannot effect any payment for claims existing at the time of the opening of bankruptcy proceedings, the debtor shall be allowed to undertake any new commitment subject to the consent of the administrator, payments may be made from the debtors assets subject to authorisation by the administrator, and the contract concluded with the debtor may not be avoided, and it may not be terminated on the grounds of the debtors failure to settle during the term of the stay of payment its debts incurred before the term of the temporary stay of payment.

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**Post-filing credit**

- 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

According to the general rule, in case of reorganisation, the debtor shall be allowed to undertake any new commitment – secured or unsecured loans or credit – subject to the consent of the administrator and priority rank is given to the secured ones.

In case of liquidation, the head of the debtor economic operator shall be restricted from entering into any contract considered to be in excess of the scope of normal operations where the economic operators assets are concerned without the prior consent and endorsement of the temporary administrator, or from entering into any other commitment, including where the debtor is compelled to perform under an existing contract.

See questions 14 and 15.

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**Set-off and netting**

- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

For the duration of the stay of payment set-off may not be applied against the debtor, however, a set-off claim may be heard in judicial proceedings initiated by the debtor and still in progress, if submitted before the time of the opening of bankruptcy proceedings.

In a liquidation proceeding only such claims can be set-off that have been registered by the liquidator as acknowledged and have not been assigned subsequent to the time of the opening of liquidation proceedings, or, if the claim has occurred at a later date, subsequent to its occurrence. The executive officers and executive employees of the debtor economic operator, their close relatives and their domestic partners, furthermore, any member of the economic operator with majority control over the debtor or the economic operator in which the debtor has majority control, may not set off their claims against the debtor.

In addition, in the case of an agreement for close-out netting concluded prior to the time of the opening of liquidation proceedings, the creditor shall notify this net claim to the liquidator, and the liquidator shall enforce this net claim. Contracts underlying close-out netting arrangements or framework contracts may be avoided or cancelled only if done concurrently.

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**Sale of assets**

- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

In case of reorganisation, the sale of specific assets out of the ordinary course of business or the entire business of the debtor is subject to the approval of the administrator.

In case of liquidation, the liquidator shall dispose of the debtors assets through public sales at the highest price that can be obtained on the market, in which case the highest bidder will acquire the assets free and clear. The liquidator shall effect the sale by way of tender or auction. The liquidator may forego the application of these procedures only upon the prior consent of the select committee, or if the estimated proceeds are insufficient to cover the costs of sale, or if the difference between the prospective proceeds and estimated costs is less than 100,000 forints. In this case the liquidator may apply other public forms of sale for the purpose of achieving a more favourable result.

If the assets to be sold include land or a farmstead, their sale shall be governed by the relevant provisions of the Act on Transactions in Agricultural and Forestry Land and the decree implementing it.

No stalking horse rules and credit bidding apply under Hungarian Law regarding insolvency proceedings.

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**Intellectual property assets in insolvencies**

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

No specific rules exist under Hungarian law regarding the IP rights in case of bankruptcy or liquidation.

According to the general rule, during bankruptcy a contract concluded with the debtor may not be avoided, and it may not be terminated on the grounds of the debtors failure to settle during the term of the stay of payment its debts incurred before the term of the temporary stay of payment, however if the given contract stipulates that the commencement of bankruptcy proceeding or liquidation proceeding establishes a right to terminate the contract, the licensor or the owner has the right to do so.

The liquidator has the right to terminate any contract of the debtor.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Bankruptcy Act does not stipulate special provisions regarding the use of any personal information or customer data collected by an insolvent company.

In accordance with the provisions of Act CXII of 2011 on the Right of Informational Self-Determination and on Freedom of Information, personal data may be processed only for specified and explicit purposes, where they are necessary for the implementation of certain rights or obligations. The purpose of processing must be satisfied in all stages of data processing operations; recording of personal data shall be done under the principle of lawfulness and fairness. The personal data processed must be essential for the purpose for which they were recorded, and it must be suitable to achieve that purpose. Personal data may be processed to the extent and for the duration necessary to achieve their purpose. Personal data may be processed only when the data subject has given consent, or when processing is necessary as decreed by law or by a local authority based on authorisation conferred by law.

### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

According to the general rule, no contracts can be rejected or terminated on the account of reorganisation. The debtor or the administrator may challenge the contract before ordinary court only in accordance with the Hungarian Civil Code and the provisions of the Code of Civil Procedure. Claims arising after the commencement of the insolvency may also be registered.

### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Bankruptcy and liquidation proceedings are non-contentious proceedings conducted exclusively by the general court of competence and jurisdiction by reference to the debtor's registered office of record on the day when the request for opening the proceedings has been submitted and by the Budapest Metropolitan Court, thus arbitration courts cannot commence insolvency proceedings, however, the administrator or the liquidator may submit a claim regarding disputes arising between the debtor and the creditor.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

A composition agreement (reorganisation plan) may be concluded if the debtor was able to secure the majority of the votes for the agreement from the creditors holding voting rights.

The composition agreement shall be made in writing and shall contain, in particular:

- a list of the creditors participating, their classification, the amounts of their claims and the number of their voting rights;
- settlement and restructuring programme approved by the creditors, and the method of execution and oversight;

- any modification in the time limits of performance; and
- the name and mailing address of each creditor.

The composition arrangement shall be signed by the parties, and by their legal representatives or proxies, and shall be countersigned by the administrator and by the select committee, if there is one.

The composition agreement shall not release non-debtor parties from liability.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

No expedited reorganisations exist under Hungarian law.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

During the opening session of the composition conference the creditors may express their refusal to support the composition proposal. If the debtor refuses to rework the composition proposal, the meeting shall be declared closed and so recorded in the minutes, and it shall be sent to the court and the supreme body of the debtor. If no composition is arranged with the creditors, or if the arrangement fails to comply with the relevant regulations, the court shall dismiss the bankruptcy proceedings and shall consequently declare the debtor insolvent and shall order the liquidation of the debtor.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

In case of bankruptcy the debtor shall notify its creditors directly within five working days following publication of the ruling ordering the opening of bankruptcy proceedings, and – furthermore – shall publish a notice in a daily newspaper of nationwide circulation and also on its website (if available) advising the creditors to register their claims within the time limit specified and to make the payment charged for the registration of claims to the payment account of the administrator appointed by the court, and to attach the documents in proof of their claim.

In case of liquidation, upon the ruling ordering liquidation of a debtor becoming final, the court shall without delay appoint the liquidator and shall order to have the abstract of the ruling ordering liquidation and the ruling on the appointment of the liquidator published in the company gazette. Publication in the company gazette shall take place in the form of display on the website of company gazette, updated on a daily basis.

Moreover, the head of an economic operator is obliged to inform the beneficiaries of the claims specified in the Bankruptcy Act regarding the opening of liquidation proceedings within 15 days from the time of opening. If the head of an economic operator does not comply with the regulations, the court shall impose a fine.

The creditors may not pursue the estate's remedies against third parties.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

In the event of any illegal action or negligence by the liquidator, the creditors' select committee and the creditors' representative may file a complaint at the court that has ordered liquidation. If the court entails the hearing of the parties or the admission of other evidence, the court shall order suspension of the measures contested. If the complaint is found substantiated the court shall overturn the measures of the liquidator and restore the original conditions, or shall order the liquidator

to revise his or her actions. If the complaint concerns the allocation of liquidation costs, the court – if so requested – may order the liquidator to provide compensation for the debtor for any liquidation costs that have been charged unlawfully.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Creditors may form a creditors' select committee for the protection of their interests and to provide representation, furthermore, to monitor the activities of the administrator and the liquidator. The select committee shall exercise the rights and entitlements conferred by the Bankruptcy Act.

Only one select committee can be appointed in respect of any one economic operator in debt. Other creditors may subsequently join in the operation of the creditors select committee. In bankruptcy proceedings, a select committee shall be deemed legitimate if comprising at least one-third of the creditors with voting rights, and if these creditors control at least one-half of the votes. In liquidation proceedings, a select committee shall be deemed legitimate if comprising at least one-third of the notified creditors and these creditors hold at least one-third of all claims of creditors entitled to participate in the composition agreement.

The select committee's powers, representation of the creditors operating the select committee, the provision of funding and the rules for the advancing and accounting of costs and expenses shall be laid down by agreement concluded by the creditors. In the process of setting up and operating the select committee, voting rights shall be distributed among the participating creditors. Decisions shall be adopted by open ballot subject to simple majority. A creditors' select committee that was established in bankruptcy may continue to function in the liquidation proceedings, if able to meet the conditions specified.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

There are no combined insolvency proceedings under Hungarian law. If any controlled member of the group is undergoing liquidation, the dominant member shall be held liable for any debt the member may have outstanding. The dominant member shall be relieved of liability if able to verify that the controlled member's insolvency did not arise as a consequence of the group's common business strategy.

The transfer of specific assets of the debtor under bankruptcy or liquidation cannot be transferred to another country, only in case of the administrator's (liquidator's) approval. For further information see question 18.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Bankruptcy and liquidation proceedings are non-contentious proceedings. The provisions of the Code of Civil Procedure shall apply to redress matters of these proceedings that are not governed under the Bankruptcy Act.

The Bankruptcy Act stipulates provisions concerning the redress options in the case of the opening of the insolvency procedure. In bankruptcy proceedings, the court decision ordering the opening of bankruptcy proceedings may not be appealed. An appeal against the decision for the refusal of the petition for the opening of bankruptcy proceedings shall be lodged within five days. No application for continuation shall be accepted upon missing the above deadline. The appeal shall be heard without delay, within a maximum period of eight

working days. In liquidation proceedings, the court decision ordering the opening of the liquidation may not be appealed.

Under Hungarian law, there is no requirement to post security in order to proceed with an appeal; however, duty shall be paid when submitting an appeal. The amount of the duty is determined by Act XCIII of 1990 on Duties.

### Claims

#### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Creditors shall make the payment charged for the registration of claims to the payment account of the administrator appointed by the court, and shall attach the documents in proof of their claim. No claim will be registered in the event of their failure to do so in due time. Claims where any payment obligation of the debtor depends on a future event need not be notified yet. The registration of claims is subject to a registration fee payable by the creditor amounting to 1 per cent of the claim – 100,000 forints maximum – to the administrator's current account. The administrator shall then categorise and register the claims. The debtor and creditors shall be informed without delay concerning the classification of claims and the amount registered, and they shall be given an opportunity to present their views within five working days. Such comments shall be decided by the administrator and the creditor and the debtor shall be notified immediately, upon which they shall have five days to submit any objection to the court concerning the administrator's action pertaining to the classification process, including the case where the administrator registered a claim of an amount other than the one notified by the creditor. The court shall adopt a decision relating to such objection in priority proceedings. The ruling may not be appealed separately. The liquidator shall register the claims against the debtor that are notified after 40 days, but within 180 days of the publication of the opening of liquidation proceedings. These claims shall be satisfied if there are sufficient funds remaining following the settlement of the debts notified duly. The general rules on the order of satisfaction shall apply to the creditors notifying their claims past the prescribed time limit.

### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

Under Hungarian law, the court may change the rank (priority) of a creditor's claim – which is determined by law, see question 33 – if the creditor appealed the administrator's decision of ranking its claim and the court rules in favour of the creditor.

### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

In the liquidation process the following priority groups of claims exist:

- liquidation costs;
- claims secured;
- claims as alimony and life-annuity payments, compensation benefits, restitution;
- claims of private individuals not originating from economic activities claims of small and micro companies;
- debts owed to social security funds, taxes;
- other claims;
- default interests and late charges, as well as surcharges and penalty and similar debts; and
- claims, other than wages and other similar benefits.

In bankruptcy proceedings the administrator shall categorise the claims as per the following:

- claims with regard to stay of payment; and

- secured and unsecured claims notified within the time limit.

### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

According to the Hungarian Labour Code, the employer shall be permitted to terminate an employment relationship by notice if undergoing liquidation or bankruptcy proceedings, thus, without stipulating differently in the contract, no claims will arise from termination. In case of different contractual obligations, the employee may submit a claim. The employer is entitled to collective redundancy according to the provisions of the Labour Code.

The employer shall be liable to pay up to six months' absentee pay due to the executive employee from the remuneration payable upon termination of his employment, if the notice of termination is delivered after the opening of bankruptcy or liquidation proceedings. Any additional sum shall be payable upon the conclusion or termination of bankruptcy proceedings, or upon the conclusion of liquidation proceedings.

### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Employers in Hungary have no obligations to offer pension plans, thus no claims arise against employers in case of insolvency proceedings. The administrator, however, is obliged to transfer the relevant data to the competent Hungarian authority, regarding employment relationships. Termination-related costs are considered liquidation costs, which have the highest priority among claims.

### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The 106/1995 (IX.8.) Government Decree on the Requirements of Environmental and Nature Protection during Liquidation and Bankruptcy Proceedings stipulates the provisions regarding environmental protection, the requirements and the manner of resolving environmental damage and contamination, furthermore, the types of expenses arising therefrom. According to the general rule the liquidator shall provide for damage and contamination of the environment proven to originate from before the time of the opening of liquidation proceedings. This means that the costs of the necessary measures to be taken – even in the lack of the debtor's assets – to eliminate dangerous waste shall be borne by the central budget of the state.

### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

In case of reorganisation, the qualified composition agreement shall decide about the survival of any liability, while in case of liquidation, after the proceeding is concluded, the economic operator ceases to exist, thus no liability survives.

### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In case of reorganisation, distribution is made in accordance with the composition plan. In case of liquidation, distribution is made in accordance with the composition plan or the decision of the court. The time of the distribution depends on the claim. In certain cases the claim can be satisfied upon maturity.

See question 33, where the rank of the claims is detailed.

### Update and trends

On 20 May 2015, the European Parliament and the Council amended EC Regulation 1346/2000 on insolvency proceedings by EU Regulation 848/2015. The new Regulation will be applicable to insolvency proceedings from 26 June 2017. The Regulation sets out EU-wide rules to establish the efficient administration of insolvency proceedings involving business activities in cross-border cases. The provisions of the new Regulation will establish the competent court, the applicable national law and recognition of court decisions.

According to a recent amendment to the Hungarian Civil Code, effective from 1 July 2016, the liability for any damage caused by the executive officer lies with the executive officer and the legal person jointly and severally only if the damage was caused intentionally.

The previous regime stipulated that if an executive officer of legal person causes damage to a third party in connection with his or her office, regardless of the intention of the executive officer, the liability lies with the executive officer and the legal person jointly and severally. This recent amendment therefore puts any third party into a more disadvantageous position when enforcing its claim against a legal person arising from such circumstances, which has a direct effect on the insolvency proceedings under Hungarian law.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The following transactions can be annulled or set aside. Contracts concluded by the debtor within five years preceding the date when the court received the petition for opening liquidation proceedings or thereafter, or his other commitments, if intended to conceal the debtors assets or to defraud any one creditor or the creditors, and the other party had or should have had knowledge of such intent. Contracts concluded by the debtor within two years preceding the date when the court received the petition for opening liquidation proceedings or thereafter, or his or her other commitments, if intended to transfer the debtor's assets without any compensation or to undertake any commitment for the encumbrance of any part of the debtor's assets, or if the stipulated consideration constitutes unreasonable and extensive benefits to a third party. Contracts concluded by the debtor within 90 days preceding the date when the court received the petition for opening liquidation proceedings or thereafter, or his other commitments, if intended to give preference and privileges to any one creditor, such as the amendment of an existing contract to the benefit of a creditor, or to provide financial collateral to a creditor that does not have any. If the contest is successful, the provisions of the Civil Code pertaining to invalid contracts shall apply. The liquidator and the creditor may request on the grounds of invalidity to have the original state restored, and to have any right registered in a public register on the asset after the alienation of the asset stricken from the records.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The administrator contest, at its discretion, any contract or legal statement the debtor has made in the absence of his approval or endorsement required, and shall initiate or open proceedings for the recovery of any payments effected unlawfully or arising out of or in connection with any unlawful claim. If the contest is successful, the provisions of the Civil Code pertaining to invalid contracts shall apply.

The creditor, and on behalf of the debtor, the liquidator may file for legal action before the court within 90 days from the time of gaining knowledge or within a one-year limitation period from the date of publication of the notice of liquidation to contest. The liquidator, on behalf of the debtor, shall be entitled to reclaim any service the debtor has provided within a 60-day period preceding the date when the court received the petition for opening liquidation proceedings or thereafter, if it was provided to give preference to any one creditor and

if such service is not usually provided under normal circumstances. Prepayment of a debt is, in particular, considered as giving preference or privileges to any one creditor.

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#### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Any creditor or the liquidator may bring action during the liquidation proceedings for the court to establish that the former executives of the economic operator failed to properly represent the interests of creditors in the span of three years prior to the opening of liquidation proceedings. Financial security may also be demanded with a view to providing satisfaction for the creditor's claims.

Any executive referred to who is able to verify that they have taken all measures within reason, that are to be expected from persons in such positions, upon the occurrence of a situation carrying potential danger of insolvency so as to prevent and mitigate the losses of creditors, and to prompt the supreme body of the debtor economic operator to take action, shall not be held responsible.

Within a 60-day limitation from publication in the company gazette, any creditor may bring action for the court to establish the liability of the debtors former executive and hence to order this executive to satisfy the debtor's claim to the extent of its claims not yet satisfied.

The court shall impose a fine upon the head of the debtor economic operator for effecting any payment in violation of the provisions of the Bankruptcy Act, or for enabling creditors to obtain satisfaction for their claims in violation of the provisions of the Bankruptcy Act. The fine shall cover 10 per cent of the amount paid out.

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#### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

If any controlled member of the group is undergoing liquidation, the dominant member shall be held liable for any debt the member may have outstanding. The dominant member shall be relieved of liability if able to verify that the controlled members insolvency did not arise as a consequence of the groups common business strategy.

Insolvency proceedings initiated against the foreign parent company abroad shall only apply to the Hungarian branch office under an international agreement or state of reciprocity or in accordance with Council Regulation 1346/2000/EC on insolvency proceedings. If the branch office is not involved in the insolvency proceedings initiated against the foreign parent company abroad under the laws of that country due to the lack of an international agreement or state of reciprocity or if the provisions of Council Regulation 1346/2000/EC apply, the general court responsible for the place where the branch office is registered shall order dissolution of the branch office ex officio on the basis of notification by the court of registry.

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#### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

If the debtor enters into an agreement with an economic operator that is under its majority control, with a shareholder or executive officer of such economic operator, or with their relatives, bad faith or gratuitous promise shall be presumed. Furthermore, bad faith or gratuitous promise shall also be presumed when a contract is concluded between economic operators that are not directly or indirectly connected by way of affiliation, but are controlled by the same person or the same economic operator.

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#### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Any assets not realised during the reorganisation or liquidation may be seized outside of court proceedings based on a contractual right.

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#### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

There are no specific corporate procedures for the liquidation or dissolution of a corporation.

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#### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

See questions 23, 26, 28, 29 and 31.

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#### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

The general rules regarding foreign judgments apply (with the provisions of the Insolvency Regulation of the EU). Hungary is not a signatory to any treaties on international insolvency or on the recognition of foreign judgments. The UNCITRAL Model Law on Cross-Border Insolvency has not been adopted and the adoption of it is not in consideration.

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**COMI**

- 48** What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

No test is officially used to determine the COMI of a debtor company or group of companies.

**Cross-border cooperation**

- 49** Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

The regulations of the EU regarding the recognition of foreign insolvency proceedings apply. In any other case, cooperation and recognition depend on bilateral treaties or on the principle of reciprocity. No court statistics are available regarding refusals.

**Cross-border insolvency protocols and joint court hearings**

- 50** In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

The Hungarian courts have not entered into cross-border insolvency protocols or other agreements to coordinate proceedings with courts in other countries, and they have not held joint hearings with courts in other countries in cross-border cases.

The Budapest Metropolitan Court shall have exclusive jurisdiction to conduct main and territorial insolvency proceedings under Council Regulation 1346/2000/EC on insolvency proceedings concerning economic operators established in a place other than Hungary.

# India

Nihar Mody and Ankit Majmudar

Platinum Partners

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

#### Legislation

The principal legislation under Indian laws with respect to corporate insolvency and reorganisations is the Companies Act, 1956 (the 1956 Act). After the enactment of the Companies Act, 2013 (the 2013 Act), various provisions of the 1956 Act have been amended and replaced – however, since the provisions in the 1956 Act dealing with corporate insolvency and reorganisations have not been replaced yet, such provisions continue to be relevant and in force. The responses set forth below refer to the provisions of the 1956 Act and the 2013 Act, which are relevant for that response, and are in force, as the provisions of the Companies Act.

Under the Companies Act, there are two types of winding up:

- winding up by the court; and
- voluntary winding up.

The provisions of the Sick Industrial Companies (Special Provisions) Act, 1985 (SICA) also provide for mechanisms for revival and rehabilitation of a sick industrial company and a potentially sick industrial company, including financial reconstruction or reorganisation. The Board for Industrial and Financial Reorganisation (BIFR) under SICA has the power to refer a company to the High Court of the relevant jurisdiction (the Court) for winding up.

The Reserve Bank of India (RBI) has introduced the corporate debt restructuring scheme (CDR) to enable creditors to jointly agree on the mechanics of restructuring a distressed company. CDR is a non-statutory, voluntary and contractual mechanism.

The RBI's 'Scheme for Sustainable Structuring of Stressed Assets' (S4A) is another optional framework for the resolution of large stressed accounts of lenders. The S4A envisages determination of the sustainable debt level for a stressed borrower, and bifurcation of the outstanding debt into sustainable debt and equity/quasi-equity instruments that are expected to provide an upside to the lenders when the borrower turns around.

The Indian parliament has recently enacted the Insolvency and Bankruptcy Code, 2016 (the Code), which seeks to overhaul the Indian corporate insolvency laws and processes. However, the substantive provisions of the Code have not been brought into force yet, although the government has commenced the process for putting the necessary infrastructure in place before operationalising the Code. Once the Code comes into effect in its entirety, the current regime relating to corporate insolvency and restructuring will be radically altered. For instance, the provisions under the SICA may be repealed and the provisions under the Companies Act will be substantially amended. A brief overview of the sweeping changes that the Code would make once it is implemented is provided in 'Update and trends'.

#### Criteria

The criterion for applicability of the insolvency provisions under the Companies Act is that the debtor must be unable to pay its debts in excess of 500 rupees. (See questions 11, 12 and 14 for details.)

The criterion for proceedings being initiated under the SICA is that the accumulated losses of a company at the end of a financial year must be equal to or greater than its entire net worth, thereby making it a 'sick company'. (See question 13 for details.)

Proceedings under the CDR mechanism can be initiated with respect to a company that has an aggregate outstanding exposure of or above 100 million rupees. A reference can be made by creditors who have a minimum 20 per cent share in the company's working capital or term finance, or by the company itself, if supported by such a creditor.

The S4A requires that an eligible account be such that the project to which it relates has commenced commercial operations, the aggregate exposure of all institutional lenders in the account is more than 5 billion rupees and the debt fulfils the test of sustainability.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The Court serves as the forum for liquidation and reorganisation proceedings under the Companies Act. Such proceedings must be initiated before the Court within whose jurisdiction the registered office of the debtor is situated. There are no other restrictions on the Court with respect to such proceedings, and it has the power to oversee such proceedings.

The BIFR is the relevant authority under the SICA for a reference relating to an industrial company (see question 13 for details). There are no restrictions on the BIFR while dealing with proceedings under the SICA, and it has the power to periodically monitor the implementation of a scheme. If the BIFR is of the opinion that rehabilitation of the sick company is not feasible and it must be liquidated, it can refer such company to the Court for liquidation, and not continue with such proceedings.

Pursuant to the provisions of the Companies Act and the Code, a National Company Law Tribunal (NCLT) has recently been constituted, and is expected to be the appropriate forum for dealing with insolvency proceedings in the near future. However, as on the date of writing, the Court continues to serve as the relevant forum for these matters.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

#### Entities

Under the Companies Act, the government may exclude certain companies from the application of its provisions. Secured creditors may choose to stay out of the winding-up proceedings and claim the amounts owed to them from the secured assets, subject to *pari passu* claims of the workmen.

#### Assets

The Companies Act and the SICA do not specifically exclude any assets from insolvency proceedings. In fact, the Companies Act gives the liquidator very wide powers with respect to taking custody of the assets

of a company in liquidation. This includes all the property, effects and actionable claims to which a company is or even appears to be entitled.

### Public enterprises

#### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Indian laws do not provide for any special insolvency procedures for government-owned enterprises, which are subject to the same procedures as non-government companies. The remedies available to the creditors of other insolvent companies will also apply to an insolvent government-owned enterprise.

However, if a government-owned enterprise is established under a special piece of legislation, such legislation may provide that its processes, and not the general law relating to insolvency, would apply to such enterprises.

### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Under the Companies Act and the Banking Regulation Act, 1949, the government or the RBI, respectively, may order the amalgamation of companies in national or public interest. The government may resort to this provision to save companies or banks and financial institutions in distress.

Additionally, the RBI categorises certain banks as 'Domestic Systemically Important Banks' every year in accordance with its Framework for Dealing with Domestic Systemically Important Banks (D-SIBs). These banks are considered 'too big to fail', and are, therefore, required to comply with greater loss absorbency requirements and higher capital requirements.

In order to ensure faster recovery of dues by banks and financial institutions, and for protection of public interest, India has enacted the Recovery of Debts Due to Banks and Financial Institutions Act, 1993 (RDB) and the Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 (SARFAESI). Under the RDB, a bank or financial institution that is owed 1 million rupees or more, can approach a debt recovery tribunal, which follows a summary procedure unlike civil courts. Under SARFAESI, a secured creditor can enforce its security to recover debts in cases of default largely without court intervention.

The S4A also deals with large financial accounts. For details, see question 1.

### Secured lending and credit (immovables)

#### 6 What principal types of security are taken on immovable (real) property?

The principal type of security taken on immovable property is by way of mortgage. Six types of mortgage are recognised in India:

- simple mortgage: where mortgage is created without transferring property to the mortgagee;
- English mortgage: where the mortgaged property is transferred to the mortgagee until repayment of mortgage money;
- mortgage by deposit of title deeds: where the act of depositing the title deeds operates as security for the mortgage;
- mortgage by conditional sale: where the mortgagor sells the mortgaged property on condition that the sale will become absolute upon default of payment by the mortgagor;
- usufructuary mortgage: where the possession and benefits of the mortgaged property are enjoyed by the mortgagee, the benefits being appropriated in lieu of the mortgage money due; and
- anomalous mortgage: any other type of mortgage apart from the ones described above.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The most commonly used forms of securities over moveable property are:

- fixed charge: used in cases of property that is quantifiable and identifiable;
- floating charge: used for property that is circulating or fluctuating in nature, such as stock-in-trade and raw material;
- hypothecation: charge is created without possession of property transferring to the creditor;
- pledge: charge requires possession of property to remain with creditor until payment of debt;
- lien: charge requires passive possession of the property until the debt is discharged; and
- mortgage: property remains with the debtor, while right over security transfers to the creditor.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

In cases of restructuring under the Companies Act, the payouts may be determined by the majority who approved the scheme, thereby making payouts to unsecured creditors dependent upon such majority's decision. See question 11 for details.

Under the SICA, once the BIFR has sanctioned a scheme, it becomes binding on all creditors. However, a Court has, in the past, disallowed the BIFR from wiping out the debt owed to unsecured creditors. Hence, the scheme cannot have the effect of erasing owed debt. To do so, consent of the unsecured creditors must be taken. Alternatively, the unsecured creditors can opt out of the restructuring process, and can enforce their claims after the restructuring is complete.

In addition, an unsecured creditor can:

- initiate proceedings before the civil court under the provisions of the Indian Code of Civil Procedure, 1908 (CPC), in order to recover its debts from defaulters;
- file an application under the RDB before a debt recovery tribunal, if the amount of debt involved in greater than 1 million rupees and if the debtor is a bank or financial institution; and
- apply to the Court for winding up of the debtor and the appointment of a liquidator, by following the process set out in question 10.

Unsecured creditors holding dishonoured cheques can also avail themselves of the special remedies under the Negotiable Instruments Act, 1881.

Under the CPC, unsecured creditors can file a petition before the civil court for the pre-judgment attachment of the debtor's property, which the civil court may grant to prevent injustice. However, the leave of the Court will have to be taken for this purpose.

Foreign creditors of Indian companies are not distinguished against Indian creditors. However, they will need to comply with the applicable provisions of the Foreign Exchange Management Act, 1999 (FEMA) in relation to remittance of debts due abroad upon repayment.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Under the Companies Act, a debtor can commence the process for its liquidation pursuant to a resolution of its members and creditors. The debtor can also file a petition before the Court for its liquidation following the process set out in question 10.

#### Effects

Upon passing of such resolution, liquidation proceedings are deemed to commence, and the debtor is required to give notice of such resolution to the Registrar of Companies.

The debtor is then required to appoint a liquidator, after which all powers of its board of directors cease. The liquidator then follows the process for dissolution of the company. The corporate state and corporate powers of the company continue until the company is dissolved.

### **Involuntary liquidations**

#### **10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

Under the Companies Act, upon a creditor commencing liquidation proceedings by filing a petition before the Court, the Court may pass an order of winding up where:

- the amount of debt is 500 rupees or above;
- the debtor has neglected to pay the debt, or has failed to secure or compound it to the creditor's reasonable satisfaction, for three weeks from the time a demand was made by the creditor;
- the debtor has not repaid the debt owed pursuant to a judicial order requiring payment; or
- based on the contingent and prospective liabilities of the debtor, the Court feels that the debtor is unable to pay its debts.

#### **Effects**

Once such a petition is admitted, the process is court-driven and is supervised by an official liquidator appointed by the Court. The debtor's board of directors loses its powers of the company's management and the liquidator assumes control over the company's assets and is empowered to continue the company's operations, subject to the Court's oversight. Various restrictions, including on disposition of the property of the company, transfer of shares or alteration in status of members are imposed during the pendency of the winding up, and these actions are permitted only with the Court's approval. The winding up concludes with the liquidation of the debtor's assets and ceasing of its business. The debtor's liabilities are then discharged to the extent possible and in the manner of priority set out in the Companies Act. Following this, the debtor ceases to exist as a corporate entity.

### **Voluntary reorganisations**

#### **11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

Under the Companies Act, a debtor can commence reorganisation proceedings by seeking the Court's approval for a scheme of arrangement. Such scheme is required to be approved by creditors or members who are a majority in number, and three-quarters by value.

The Court supervises the entire process of the reorganisation, and with respect to the scheme, generally considers whether it:

- is fair and is in the interests of the company, its creditors and its shareholders;
- complies with the procedural requirements under the Companies Act; and
- violates any principles of public policy.

Once the Court sanctions the scheme, it is implemented. The Court will also give notice to the regional director, registrar of companies and the Income Tax Department and consider their representations before sanctioning the scheme.

Under the CDR scheme, a debtor can initiate proceedings if the criteria set out in question 1 are met. Once the relevant authority starts considering a restructuring proposal, there is a 90-day restriction on the creditors involved in the process from initiating other proceedings for recovery of debt, which can be extended to 180 days. Once the restructuring plan is approved in accordance with the scheme, it is given effect.

### **Involuntary reorganisations**

#### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

Under the Companies Act, a creditor of a company can file a scheme of arrangement before the Court and commence proceedings for such reorganisation of such company. The requirements and effects for such reorganisation are similar to those when a debtor itself commences such proceedings, as set out in question 11.

Under the SICA, upon fulfilling the criteria for becoming a sick company as set out in question 1, the debtor must make a reference to the BIFR for its revival and rehabilitation. The BIFR will then make an inquiry to determine the debtor's sickness and depending on which option is more viable, either order its revival (in which case an operating agency will draft a scheme, which will be implemented upon BIFR's approval) or its winding up (in which case the provisions of the Companies Act will apply).

Under the CDR Scheme, a creditor can initiate proceedings if the criteria set out in question 1 are met. The effect of such a proceeding is similar to a proceeding initiated by the debtor, as set out in question 11.

Once a debtor is eligible as detailed in question 1, the S4A mechanism requires the creditors to submit a resolution plan (approved by 75 per cent of the creditors in value and 50 per cent in number) to an Overseeing Committee, which will review the plan's viability and ratify it. Once such ratification is obtained, the resolution plan will be binding on all creditors.

### **Mandatory commencement of insolvency proceedings**

#### **13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

The Companies Act does not mandate commencement of insolvency proceedings by a company, and it may carry on business while insolvent. However, in the course of winding up, the Court may require officers of the company who have acted fraudulently, or committed misfeasance or breach of trust during liquidation proceedings, to make good the loss so caused.

Under the SICA, an industrial company which at the end of a financial year has:

- accumulated losses equal to or exceeding its entire net worth, must file a reference with the BIFR, following which, schemes for its revival and rehabilitation are formulated; and
- accumulated losses eroding 50 per cent or more of its peak net worth during the immediately preceding four financial years, must file a report with the BIFR and hold a shareholders' meeting to consider such erosion.

Non-compliance may result in imprisonment or fine for the directors and officers in default, or both.

### **Doing business in reorganisations**

#### **14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

Under the Companies Act, a debtor can continue to carry on its business during a reorganisation. There is no specific bar on the debtor with respect to the use or sale of its assets, and its day-to-day operations continue to be carried on by its management. However, the Court has the power to supervise the carrying out of the reorganisation, and to make modifications to the scheme as it deems fit.

Under the SICA, at any time during an inquiry, a company may carry on business after obtaining the approval of the BIFR. During the pendency of a rehabilitation proceeding, the BIFR may direct the company to seek its approval for disposal of assets. In addition, the BIFR may declare that the operation of, and rights, privileges, obligations and liabilities under any contract, assurance of property, award or other instrument in force, to which such company is a party, shall remain suspended or be enforceable in such manner as the BIFR may specify.

In the CDR mechanism, the debtor's business is not interrupted, but its management is supervised by an administrative body. Assets, especially those for which dues are owed to the debtor, are closely monitored and classified for risk. The CDR Standing Forum is given rights to supervise the debtor's business activities, and creditors who had to forego their dues during the restructuring will be entitled to

recompense upon its completion. (For details, see question 28.) When the CDR process has been initiated, the directors of the debtor are not allowed to resign from the board of directors during the restructuring period.

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### Stays of proceedings and moratoria

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#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

Once an order of winding up has been passed or a liquidator has been appointed under the Companies Act, no suit or legal proceeding is allowed to be commenced or proceeded with against the company, without the Court's approval (apart from a few specific exceptions). Consequently, enforcement of claims by creditors is also regulated during such period. Creditors are required to prove their debt to the liquidator within 14 days of being notified about the winding up of the debtor, failing which, a creditor can apply to the Court for appropriate relief.

With respect to reorganisations, there is no automatic prohibition on continuation of legal proceedings or enforcement of claims. However, the Court has wide powers to pass such an order in appropriate cases.

During the pendency of rehabilitation proceedings under the SICA, none of the following can lie or be proceeded with without the BIFR's approval (subject to a few exceptions):

- proceedings for winding up or execution, distress or the like against any of the company's properties;
- appointment of a receiver;
- suit for the recovery of money or for the enforcement of any security; and
- suit for the recovery of any guarantee or advance.

Under the CDR mechanism, the debtor-creditor agreement may provide for 'standstill' provisions whereby the debtor and the creditor undertake not to take recourse to other legal proceedings during the standstill period.

The S4A mechanism also provides for a limited standstill clause.

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### Post-filing credit

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#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Under the Companies Act, during a liquidation proceeding, a liquidator may, subject to the Court's approval, raise requisite interim finance, on the security of the company's assets. However, obtaining interim finance is not specifically regulated during a reorganisation proceeding.

Under the SICA, during the pendency of rehabilitation proceedings, the company or a financial institution intending to provide financial assistance can make an application to the BIFR and agree to an arrangement for continuing the operations of the company. The scheme for rehabilitation may also provide for financial assistance to be obtained from the government, banks or public financial institutions, etc.

Under CDR, during the consideration of a CDR scheme, the debtor may obtain additional finance subject to certain conditions, including those on source and use of funds. Priority in repayment is to be given to the additional finance provider.

There is no express provision giving priority to interim finance provided under the Companies Act and SICA.

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### Set-off and netting

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#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

There is no specific right of set-off or netting provided in case of restructuring under the Companies Act or SICA.

In the case of insolvency under the Companies Act, creditors may exercise rights of set-off in the same manner as provided under the insolvency laws applicable to individuals. For such a right to apply,

the claims shall be mutual and commensurable, which means that the claims must exist between the same parties in the same right.

However, there is no automatic setting-off, and proof of debt is necessary. For the purpose of set-off:

- the rights of the parties are fixed as on the date of commencement of winding up, and a sum due to a person will not be allowed to be set off against a liability created against the person post such date; and
- the sums involved in the set-off must be ascertainable.

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### Sale of assets

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#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

Under the Companies Act, during a liquidation proceeding, a disposal of assets may be void if effected without the Court's approval. In practice, the Court may impose certain conditions while approving such disposal. There are no specific provisions dealing with stalking horse or credit bids, but since the liquidator has broad powers of management, if such transactions are in the interest of the company, the liquidator may enter into such transactions on behalf of the company, subject to the Court's oversight.

There are no specific provisions with respect to sale of assets, stalking horse bids or credit bidding, during a reorganisation proceeding.

It is to be noted that in case of the sale of assets by the creditor to third-party purchasers, particularly in case of in specie distribution, the purchaser will not acquire the assets 'free and clear', but subject to the encumbrances attached to the assets sold. This is because the interest transferred to the purchaser is limited to what the creditor is capable of passing at the time of transfer.

Under the SICA, the BIFR may provide for sale of the whole or part of the industrial undertaking in a scheme.

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### Intellectual property assets in insolvencies

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#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

There is no automatic right of an IP licensor or owner to terminate a debtor's use during an insolvency proceeding under Indian laws. However, under the Companies Act, after a winding-up order, the liquidator has the power to take into custody or control all the property, effects and actionable claims to which the company is or appears to be entitled, which would include IP rights. The liquidator can take all actions with respect to the IP rights in the interest of the company.

Although the SICA does not contain provisions dealing with the use of IP, the scheme of rehabilitation may provide for the manner of dealing with the IP rights of the company.

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### Personal data in insolvencies

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#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

Under Indian law, there is no provision regulating the use of personal data in insolvencies. In reorganisations, the transferor's assets are vested on the transferee upon the completion of the purchase, which would include personal data.

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**Rejection and disclaimer of contracts in reorganisations**


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**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

Under the Companies Act, there is no specific provision for disclaimer of an unfavourable contract during reorganisation. However, during the pendency of liquidation proceedings, the liquidator (and not the debtor) may, with the Court's approval, disclaim an onerous property, including an unprofitable contract. From the date of such disclaimer, the rights, interest and liabilities of the company with respect to the disclaimed property would terminate. However, such disclaimer shall not affect the rights or liabilities of any other person, except as may be necessary to release the company and its property from liability. The liquidator is not allowed to disclaim a property if an application by an interested person has been made to him or her to decide whether or not a property will be disclaimed, and the liquidator has not, within a specified period, responded to such person. After the commencement of the liquidation proceeding, any person injured by such disclaimer is considered the company's creditor for the compensation or damages payable. There are no specific provisions dealing with the effect of a debtor breaching a contract after initiation of insolvency proceedings.

Under the SICA, the BIFR may suspend contracts or other instruments of a sick company or to which such company is a party during the pendency of proceedings before it, for a maximum period of seven years.

Under the CDR scheme, while there is no provision for a debtor to disclaim a contract, a lender is required to inform the appropriate authority about any proposed action which it proposes to take with respect to the CDR scheme. The debtor and the lender may agree to incorporate a provision in their agreement that restricts them from initiating any action against the other during the pendency of the CDR mechanism.

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**Arbitration processes in insolvency cases**


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**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Under Indian laws, insolvency and winding-up proceedings are non-arbitrable. However, in the event a liquidator has adopted a contract to which the debtor is a party and which has an arbitration clause, the liquidator is empowered to act on behalf of the debtor if such contract is sought to be enforced by, or against, the debtor.

Also, if a debtor is party to a contract containing an arbitration clause, and a dispute arises under that contract that is material to the insolvency proceedings, a court may refer such dispute to arbitration in appropriate cases.

Any arbitration proceeding is considered a 'legal proceeding', and is thus stayed once an insolvency proceeding has commenced and the moratorium (as mentioned in question 15) has been imposed.

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**Successful reorganisations**


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**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

Under the Companies Act, the usual features of a reorganisation plan include the rationale for the plan, capital structure, transfer of assets and liabilities, contracts, employees, legal and tax proceedings, accounting and tax treatment, conditionality and intellectual property. For the plan to be approved, it must be presented by the company or its members or creditors to the Court and be sanctioned by 75 per cent of the number of members or creditors present and voting.

Under the SICA, a scheme is prepared by an operating agency appointed by the BIFR, and generally includes provisions relating to

transfer of the business, assets, etc, alteration of charter documents, reduction of interest or rights of shareholders of the sick company, method of sale of assets, transfer or issue of shares. If such scheme involves the debtor's amalgamation, a resolution with 75 per cent approval must be passed by the shareholders of the other company. If the scheme involves financial assistance to the debtor, it must be circulated to every financier within 60 days of the approval to the scheme.

Secured creditors and unsecured creditors are generally treated as two separate classes in reorganisation plans.

In the CDR mechanism, the CDR Cell submits a preliminary report to the CDR Empowered Group, based on which the latter approves the scheme.

A resolution plan in the S4A mechanism must not grant fresh moratorium on the principal amount or the interest, or an extension of the repayment schedule, and the debt must be converted into equity or redeemable cumulative optionally convertible preference shares or debentures.

The release of non-debtors parties from liability depends on the reorganisation plan.

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**Expedited reorganisations**


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**24 Do procedures exist for expedited reorganisations?**

There is no provision for expedited reorganisations under Indian law.

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**Unsuccessful reorganisations**


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**25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

Under the Companies Act, if the scheme is not approved by the requisite majority as set out in question 11 or by the Court, it will not be implemented. Further, under Indian laws, the Court has to consider whether the scheme is fair, just and reasonable and is not contrary to any provision of law. Thus, if the Court, while sanctioning a scheme, feels that the overall structure of the scheme is not just and reasonable, it may make an order rejecting the scheme, in which case the reorganisation will be unsuccessful. In the case of non-compliance with the reorganisation plan by the debtor, the Court may order the liquidation of the debtor, apart from initiating action for contempt of court.

Under the SICA, the BIFR has the power to modify and amend the scheme, as well as to monitor the implementation of the scheme. If the debtor fails to perform the plan, the BIFR may refer it for liquidation and impose other penalties.

Under the CDR mechanism, the CDR Empowered Group may decide to terminate the scheme in the event its continuation is not considered viable. This would allow creditors to raise their claims against the debtor, as the standstill imposed earlier would cease to operate.

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**Insolvency processes**


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**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

Debtors are required to file a list of creditors with the Court, and send to such creditors a notice of presentation of the petition (in case of involuntary liquidations), stating the amount of debt or claim against such creditor's name. The liquidator is then required to prepare a report for submission to the Court. The Court may constitute a committee of inspection (CoI) (for details, see question 28) to act with the liquidator. The CoI may inspect the accounts of the liquidator at reasonable times.

The liquidator is required to maintain proper books containing entries or minutes of meetings. A creditor or contributory may inspect such books.

A general meeting of the company is called at the end of each year from the commencement of liquidation proceedings, to update creditors about the proceedings. Such meeting is to be called by an advertisement published in the Official Gazette and also in newspapers circulating in the location where the debtor's registered office is situated. At such meetings, the liquidator is required to present an

account of the liquidation upon completion showing how it has been conducted and how the debtor's property has been disposed. Records of the occurrences at such meetings are to be maintained for inspection by creditors.

Creditors are not permitted to pursue the estate's remedies for this purpose. (For details, see question 27.)

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

The Companies Act does not specifically provide the creditors with a right to pursue an estate's remedies on their own. However, in the case the liquidator has no assets to pursue a claim, he or she may use funds or advances provided by the government or creditors to pursue the estate's remedies, with Court approval. These funds will be recouped out of the debtor's assets in priority to other debts.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Under the Companies Act, in the case of liquidation by the Court, the Court may order the constitution of a CoI, which consists of up to 12 persons (in involuntary liquidations) and five persons (in involuntary liquidations), being the debtor's creditors and contributories. The CoI has the power to inspect the accounts of the liquidator.

The CDR Standing Forum is a creditors' committee formed under the CDR mechanism. It is a self-empowered body, which lays down policies and guidelines, and monitors the progress of the CDR.

There is no bar on the creditors retaining advisers, and the actual out-of-pocket costs incurred by the creditors for this purpose may be paid out of the debtor's assets.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Under Indian laws, each company (whether it is a part of a corporate group or otherwise) is a separate legal entity. Thus, insolvency proceedings of each company are conducted separately, and assets and liabilities of group companies are generally not pooled for distribution purposes (except certain instances where courts lift the corporate veil). Also, assets cannot be transferred from an administrator in India to an administrator in another country without the approval of the Court and the RBI.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Under the Companies Act, appeals from orders of the Court with respect to insolvency proceedings lie in the same manner as appeals from other matters before the Court. The Supreme Court may be appealed to in case the matter involves a substantial question of law, or if the Supreme Court considers it to be a fit case for appeal.

Under the SICA, appeals from an order of the BIFR lie to the Appellate Authority for Industrial and Financial Reconstruction.

### Claims

#### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Under the Companies Act, in case of winding up, creditors are required to prove their debt to the liquidator. The claim by the creditors must be submitted in the manner of an affidavit verifying the debt owed. If the liquidator is not satisfied with the proof of debt, he or she may reject it in whole or in part. The creditor may appeal against the liquidator's decision to the Court. Once the list of creditors is assembled, it cannot be varied without a Court order.

Creditors can transfer the debt owed to them, unless the scheme provides otherwise. However, the mere right to sue cannot be traded. The CDR mechanism also contains certain conditions that must be fulfilled before claims can be transferred.

Claims for contingent debts are admitted in the same manner as current debts. For unliquidated debt, the value of the debt will be estimated as on the date of the winding-up order. Interest accrued until the date of the winding-up order can be claimed by creditors.

### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

In the case of winding up, the Court has the jurisdiction to entertain any question of priorities. The grounds may be based on law or fact. The Court may reject the claims of creditors whom it considers have, or are found to have, been given a 'fraudulent preference'. This could also occur in cases where such fraudulent preference is alleged and proved. Other creditors who may not receive payment are detailed in question 39.

In the event of the assets of the debtor being insufficient to satisfy the liabilities, the Court may order the expenses of liquidation to be paid in such order of priority as it thinks just.

In addition, the liquidator is empowered to pay any class of creditors in full, upon such an application by a creditor or contributory, with the Court's sanction.

### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

In liquidations, the order of the major priority claims is as follows:

- debts due to secured creditors and workmen's dues (treated *pari passu*);
- costs, charges and expenses of liquidation;
- preferential payments including:
  - government and statutory dues;
  - wages and salaries of employees;
  - accrued holiday remuneration;
  - employer's contribution in employee insurance plans;
  - compensation and liability under labour legislation;
  - employee dues with regard to provident funds, pension funds, gratuity funds, etc; and
  - dues for investigations ordered against the debtor;
- unsecured creditors; and
- shareholders.

Dues payable under the Employees Provident Fund and Miscellaneous Provisions Act, 1952 have been given priority over all other dues in the case of liquidation. In addition, certain state government claims (eg, sales tax) may be given priority over secured creditors.

Under CDR, claims of lenders providing additional finance rank senior to claims of existing lenders.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Termination of employment of a workman must be in accordance with the provisions of the Industrial Disputes Act, 1947. If the employee is not a workman, termination of employment must be in accordance with the employment contract.

In a liquidation, when the employment of workmen is terminated, their dues would include wages, accrued holiday remuneration, sums due under gratuity, provident and pension funds, etc. Additionally, employee claims are also given preferential treatment (as discussed in question 33) and their dues would include salary, compensation awarded under the Employees' State Insurance Act, 1948, sums due under gratuity, pension and provident fund, etc.

In a restructuring, if the interests of the employees are not safeguarded, they may object to the scheme being approved by the Court. The SICA also permits the removal of a director in case the accumulated losses of the company are greater than 50 per cent of its net worth in the previous four years. Directors so removed are not entitled to any compensation or damages for termination.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

The sums due to employees in relation to pension funds are one of the priority claims in the event of liquidation. Additionally, as discussed in question 33, provident fund dues (which include pension funds) are given priority over all other dues.

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Indian laws do not specifically distinguish environmental cases in insolvency proceedings. In general, in the case of damage to the environment, the company and persons directly in charge of, or responsible for, the conduct of the company's business are held liable for the damage and penalised accordingly.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

The liabilities during a reorganisation under the Companies Act, SICA and CDR continue to survive in accordance with the scheme. However, at the end of the winding-up proceedings under the Companies Act, none of the liabilities survive once the debtor is dissolved, subject to the Court not declaring the dissolution void within two years, upon such an application.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In liquidation, payments to creditors of a company will be made in the order of priority set out in question 33.

Once a reorganisation is completed under the Companies Act or the SICA, the assets are distributed to the creditors in accordance with the scheme. (See questions 12 and 13 for details.)

Under the CDR mechanism, once the financial performance of the debtor is more than the earnings before interest, taxes, depreciation and amortisation (EBIDTA) projections for two years, it will exit the CDR system and make the payments owed by it.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The following transactions of an insolvent company may be set aside:

- fraudulent preference: any transfer of property undertaken within six months prior to the company's winding up that would give any fraudulent preference to any persons may be declared void by the Court;
- voluntary transfer: any transfer of property made within one year before the winding up that was not undertaken in good faith and for good consideration in the ordinary course of business is void against the liquidator;
- transfer for the benefit of all creditors: any transfer or assignment by a company of all its property to trustees for the benefit of creditors is void; and
- floating charge: a floating charge on the property of a company created within 12 months preceding the commencement of winding up is invalid, unless the company was solvent immediately after creating the charge.

In the case of winding up by the Court, any transaction purporting to dispose of the property (including actionable claims) or transfer of shares of the debtor or alteration the status of its members made after the commencement of winding up may be void if effected without Court approval. In addition, any onerous property may be disclaimed with Court authorisation. (See question 21.)

In reorganisations, while there are no provisions to annul or set aside transactions, certain proceedings may be temporarily set aside. (See question 15.)

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The time period for determining whether a transaction by an insolvent debtor may be annulled varies in accordance with the nature of the transaction. (See question 39.)

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### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The Companies Act imposes liabilities on the officers and directors of a company in the case of default in compliance with obligations during, and sometimes, prior to, liquidation proceedings. For instance, among other things, it provides for imprisonment or fine, or both, in the event a person has:

- defaulted in preparing the statement of affairs or the declaration of solvency;
- falsified books of the company or maintained improper accounts;
- fraudulently conducted business; and
- induced another to give credit to the company under false pretence or fraud, or transferred the company's property to defraud the creditors, or concealed such property from creditors.

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### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

See question 29.

### Update and trends

The plethora of laws and institutions regulating insolvency and restructuring in India has resulted in multiplicity of proceedings, thereby delaying the effective and timely recovery of loans and the revival and rehabilitation of companies. The Indian legislature has recently enacted the Insolvency and Bankruptcy Code, 2016 (the Code), with a view to creating a unified framework of laws dealing with insolvency. The Code also proposes to amend certain portions of the Companies Act, 2013 and the Sick Industrial Companies (Special Provisions) Repeal Act, 2003 (which repeals the SICA, but has not been notified as yet), among others.

However, the substantive provisions of the Code have not yet come into force. To date, only certain provisions of the Code, dealing with the establishment, accounts and audit of the Insolvency and Bankruptcy Board of India (the Board) and the power of the government to make rules and issue directions have been notified. Typically, once the necessary infrastructure under a new legislation is set up, the substantive provisions are brought into force. The rest of the provisions are, therefore, likely to be notified in due course. The following is a brief overview of the insolvency resolution mechanism under the Code:

- applicability: The Code applies to companies, limited liability partnerships, partnership firms and individuals, where the defaulted debt is 100,000 rupees or more, and provides for separate mechanisms for insolvency resolution for corporate persons, and individuals and partnership firms. The Code does not apply to financial service providers;
- timeline for insolvency resolution under the Code: The Code provides that the insolvency resolution process for corporate persons will be completed within 180 days from the date of admission of an application to initiate such a process. This limit may be extended to 270 days in certain circumstances. The Code also provides for a fast-track mechanism in certain cases, wherein the insolvency resolution process is required to be completed in 90 days;
- stages of resolution: There are two stages to the process under the Code:
  - insolvency resolution process (IRP): Creditors assess the viability of continuing the debtor's business, and possible solutions for its revival; and
  - liquidation process: Winding-up proceedings are initiated in case the continuance of the debtor's business is not considered viable;
- administrative bodies for resolution: Several bodies have been appointed to manage the IRP:
  - the Insolvency and Bankruptcy Board of India: This is responsible for overseeing the functioning of entities created under the Code;
  - insolvency resolution professionals: These are responsible for conducting the IRP, taking over the management of a company, assisting creditors in the collection of relevant information and managing the liquidation process;
  - insolvency professional agencies: These are responsible for enrolment, conducting examinations, certifying and enforcing a code of conduct for insolvency resolution professionals;
  - information utilities: These are responsible for collecting, collating and disseminating financial information related to debtors in centralised electronic databases; and
  - the National Company Law Tribunal (NCLT): This is the adjudicating authority for corporate insolvency and liquidation. Appeals from NCLT orders lie to the National Company Law Appellate Tribunal and thereafter to the Supreme Court of India; and
- steps of insolvency resolution: The following are the steps followed for an IRP under the Code:
  - commencement: A financial creditor (for a financial debt) or an operational creditor (for an operational debt) or the debtor initiates the IRP before the NCLT;
  - moratorium: There is a moratorium on certain actions against the debtor for the period of the IRP;
  - appointment of resolution professional: A resolution professional is appointed to administer the IRP;
  - creditors' committee and revival plan: The resolution professional identifies the financial creditors and certain operational creditors and constitutes a creditors committee. The creditors' committee considers proposals for the revival of the debtor;
  - liquidation: The debtor may be put into liquidation in the event a 75 per cent majority of the creditors' committee so resolves, or the creditors' committee does not approve a resolution plan within 180 days, or the NCLT rejects the resolution plan submitted to it, or the debtor contravenes the resolution plan and an affected person makes an application to the NCLT; and
  - priority in payments: After the costs of insolvency resolution, secured debt together with workmen dues for the preceding two years rank highest in priority. Government dues stand below the claims of secured creditors, workmen dues, employee dues and other unsecured financial creditors.

As detailed above, most of the provisions of the Code have not been notified yet, and it remains to be seen when the Code is made operational in its entirety.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

As stated in question 39, there are restrictions on giving fraudulent preference to any person. Thus, if a claim results in such preference, it may be annulled.

Further, claims may be disallowed by the Court if they relate to transactions that:

- have not been entered into in good faith, or for inadequate consideration; or
- are not in the ordinary course of business.

An insider or a non-arm's-length creditor may have to prove that his or her claim is bona fide before it is allowed in an insolvency proceeding.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

As mentioned in question 5, under SARFAESI, a secured creditor can enforce its security to recover debts in cases of default, outside of court proceedings. However, such action can only be initiated by banks and financial institutions (which are secured creditors), who have given 60 days' written notice to a debtor about discharging its liabilities. If the debtor fails to comply with the notice, SARFAESI empowers such

secured creditors to take possession of, sell, lease, assign or manage the security for the loan.

For dues with respect to moveable property, the creditor has the rights of lien and resale, in the event he or she retains possession of the property.

For dues with respect to immovable property, the right of resale is greatly restricted, but is permissible.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

The Companies Act contains provisions for voluntary liquidation or dissolution of a solvent company – see question 9 for details. The primary difference between a voluntary liquidation and an involuntary liquidation (detailed in question 10) is the level of supervision by the Court. The appointment of a liquidator in a voluntary liquidation is by the company itself, whereas in the case of an involuntary liquidation, the Court appoints a liquidator. The procedure for involuntary liquidation is detailed in question 10.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

When the affairs of the company have been completely wound up or when the liquidator is of the opinion that he or she cannot proceed with

the winding up for want of funds or other reasons, the Court makes an order for dissolution of the company. See questions 9 and 10 for details.

A scheme of reorganisation under the Companies Act is effective once the certified copy of the order of the Court sanctioning the scheme is filed with the Registrar of Companies. The Court has the power to supervise the carrying out of the scheme or make modifications to the scheme for the proper working of the arrangement.

Under the SICA, once the scheme is sanctioned by the BIFR, it is implemented.

For the conclusion of a CDR proceeding, see question 38.

The S4A mechanism concludes once the debt is converted to other instruments, as detailed in question 23.

#### International cases

**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Foreign decrees are classified into two categories under Indian law – decrees from reciprocating territories and from non-reciprocating territories. Reciprocating territories are those notified by the government as ‘reciprocating’ under the CPC, and all other territories are ‘non-reciprocating’.

Foreign decrees passed by superior courts of reciprocating territories can be executed in the same manner as a decree passed by the domestic courts under the CPC. If the decree is of a court in a non-reciprocating territory, the relevant party would have to file a fresh civil suit on that foreign decree or on the original underlying cause of action or both, in a domestic court of competent jurisdiction.

Decrees of both reciprocating and non-reciprocating territories, however, become inconclusive and, consequently, unenforceable in the following circumstances where it:

- has not been pronounced by a court of competent jurisdiction;
- has not been given on the merits of the case;
- is founded on an incorrect view of international law or a refusal to recognise the law of India;
- is opposed to natural justice;
- has been obtained by fraud; or
- sustains a claim founded on a breach of any law in force in India.

Any foreign decree falling within the above criteria cannot be the basis of a winding-up petition as it does not constitute a debt due. Conversely, a winding-up petition can be maintained on a valid foreign decree even without it being executed.

Foreign creditors of Indian companies are not distinguished from Indian creditors. However, they will need to comply with the applicable provisions of the FEMA in relation to remittance of debts due abroad upon repayment.

While India has not adopted the UNCITRAL Model Law, the Code provides for the execution of bilateral treaties with other countries for enforcing its provisions.

#### COMI

**48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

The concept of COMI is not recognised in India. See question 2 for details on the jurisdiction of courts involved in the insolvency process.

#### Cross-border cooperation

**49 Does your country’s system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

The Companies Act provides that a company incorporated outside India but carrying on business in India may be wound up as an unregistered company once it ceases to carry on business in India. Hence, in the case the foreign company is undergoing insolvency proceedings, its Indian arm would be affected only if its business in India ceases.

Other than the provisions for execution of a foreign decree detailed in question 47, there are no other provisions for cooperation between domestic and foreign courts. As discussed in questions 22 and 47 respectively, certain matters relating to the institution, etc, of insolvency proceedings are non-arbitrable in India. A foreign judgment breaching Indian law will not be enforceable in India. Hence, even foreign arbitral awards on such matters will not be recognised in India.

#### Cross-border insolvency protocols and joint court hearings

**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

India is not a party to any cross-border insolvency protocols.

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# Indonesia

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

Bankruptcy and suspension of debt payments are regulated by Law No. 37 of 2004 concerning Bankruptcy and Suspension of Debt Payments (the Bankruptcy Law).

The Bankruptcy Law provides two main procedures for companies having financial difficulties, that is, bankruptcy and suspension of debt payments.

### Bankruptcy

Bankruptcy proceedings is pronounced by the court if there is a bankruptcy petition filed by either the creditor or the debtor itself in which it can be proven that the debtor has at least two creditors (plurality of creditors); and at least one of the two debts is due and payable. The objective of the bankruptcy procedure is to impose a general attachment over the assets of the bankrupt debtor for the purpose of satisfying the claims of the creditors.

After bankruptcy declaration, a bankrupt debtor still has the right to submit a composition plan to its creditors for approval of the creditors and for ratification by the court. In the event that, following its bankruptcy declaration by the court, no composition plan is submitted by the debtor to the creditors, a composition plan is submitted but subsequently rejected by the creditors, or a composition plan is submitted and subsequently approved by the creditors but is not ratified by the court, the bankruptcy estate is in the state of insolvency.

### Suspension of debt payments

The debtor or the creditors can apply for a suspension of debt payments if the debtor either cannot pay its debts or foresees that it will not be able to pay its debts. The suspension of debt payments procedure is provided for a debtor that faces temporary liquidity problems and is unable to pay its debts but may be able to pay them some time in the future. It provides the debtor temporary relief in order for it to reorganise and continue its business, and ultimately to satisfy its creditors' claims. The debtor is required to submit a composition plan for the approval of the creditors and for ratification by the court. The rejection of the composition plan by the creditors or its non-ratification by the court or a failure to implement it will result in the bankruptcy declaration of the debtor.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The court that has jurisdiction to hear and examine the bankruptcy and suspension of debt payments cases in Indonesia is the commercial court. There are currently five commercial courts across Indonesia with divided jurisdictions.

There is no restriction that may be dealt by the commercial court. The commercial court only hears and decides on bankruptcy and suspension of debt payment petitions (as well as any civil claim related to the bankruptcy estate or proceedings) and disputes related to intellectual property rights.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

There is no exclusion on the entities that can be declared bankrupt or granted suspension of debt payments, but there are initiation requirements for certain entities. Petition against the following can only be submitted by the Financial Services Authority:

- banks;
- security houses (among others: security companies, stock exchange, clearing and guarantee institution, or securities depository and settlement institution);
- insurance, reinsurance, and pension fund companies; and
- state-owned enterprises carrying out public interest business;

Article 50 of Law No. 1 of 2004 concerning Wealth of State restricts attachment on the state's assets.

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Petition against state-owned enterprises carrying out public interest business can only be filed by the Minister of Finance. There are no specific procedures for filing a petition against public enterprises, the general procedures mentioned above apply.

## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No.

## Secured lending and credit (immoveables)

### 6 What principal types of security are taken on immoveable (real) property?

Under Indonesian Law, types of security that can be encumbered over an immoveable property are as follows:

- mortgage: a land mortgage, which is subject to the Law No. 4 of 1996 concerning mortgages, constitutes a charge on the land itself and on all buildings and other fixtures attached to it; and
- hypothec: registered vessels are classified as immoveable assets and can be secured by way of hypothec pursuant to the provisions of Law No. 17 of 2008 on Shipping.

## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

The following are types of security that can be encumbered over a moveable property:

- pledge: A pledge requires the delivery of the pledged goods from the debtor to the creditor. The consequence of this is that a pledge

can only be created upon moveable (tangible and intangible) property. Intangible property that can be pledged includes shares, bank accounts, and rights in intellectual property;

- a fiduciary transfer of ownership and fiduciary assignment of rights: A fiduciary transfer of ownership for security purposes may be exercised upon moveable property. A fiduciary transfer of ownership does not require the physical delivery of the goods; and
- warehouse receipt: A warehouse receipt that has been issued by a warehouse manager that has been approved by the Warehouse Receipt System Supervisory Board, for specific commodities (ie, grain, rice, corn, coffee, cocoa, pepper, rubber, seaweed, rattan, salt, gambier, tea, copra or tin, which can be stored for at least 3 months; meet certain quality standard; and meet a minimum quantity of goods kept) shall serve as ownership document and can be used as debt security fully, without requiring other collateral.

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#### Unsecured credit

- 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

The bankruptcy is a general attachment of the debtor assets. Unsecured creditors are entitled to receive payment in prorata basis after payment to secured creditors and preferred creditors (taking into account the ranking order of the claim). The process and time line will follow the bankruptcy proceedings in general. Pre-judgment attachments are available upon request of petitioning creditors at the time the petition is filed, but the intent is to avoid the assets being transferred by the debtor. No special procedures apply to foreign creditors; however, the time limit for the submission and verification of claim from foreign creditors shall not apply, if such domicile of foreign creditors prevents them from reporting themselves beforehand.

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#### Voluntary liquidations

- 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?**

Liquidation (including voluntary one) is regulated under Law No. 40 of 2007 concerning Limited Liability Companies (the Company Law), voluntary liquidation is based on a resolution of the general meeting of shareholders of the company.

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#### Involuntary liquidations

- 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

A debtor may be placed into involuntary liquidation based on a court order or because of bankruptcy proceedings.

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#### Voluntary reorganisations

- 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

Financial reorganisation is similar to suspension of debt payments under Indonesian law. A debtor may submit a petition of suspension of debt payments to the commercial court if the debtor is not or will not be able to pay its debts that have been due and payable.

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#### Involuntary reorganisations

- 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

Creditors may submit a petition of suspension of debt payment if the creditors foresee that the debtor will not be able to continue to pay its debts, in order to provide an opportunity for the debtor to offer a composition plan to the creditors.

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#### Mandatory commencement of insolvency proceedings

- 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

There is no provision under Indonesian law requiring a company to commence bankruptcy or suspension of debt payment proceedings. Any bankruptcy or suspension of debt payment proceedings shall be voluntarily commenced by the debtor itself or by the creditors.

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#### Doing business in reorganisations

- 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

##### Bankruptcy

The receiver of a bankrupt debtor can continue the business of the bankrupt debtor to the extent it may increase the value of the bankruptcy estate. The counterparty to an agreement under which mutual obligations must be performed can ask for confirmation from the receiver, within a specific time frame, that the obligations will be fulfilled. If there is no agreement on the time frame, the supervisory judge will decide on a time frame. If confirmation is given, the receiver must provide security for performance of the obligation. However, this does not apply to agreements under which the bankrupt debtor must personally perform an obligation (for example, a contract under which an artist is required to paint a portrait). The receiver shall have the authority for the use or sale of assets, and the sale of assets must be made through a public sale. The continuation of the company's business is supervised by the supervisory judge. The powers and authorities of directors shall be taken over by the receiver.

##### Suspension of debt payments

Under the suspension of debt payments procedure, the company continues its business activities under the joint management of the administrator and the board of directors. The supervisory judge supervises the continuation of the business.

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#### Stays of proceedings and moratoria

- 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

##### Bankruptcy

By declaration of the debtor's bankruptcy, any ongoing civil proceedings, in which the plaintiff requests for fulfilment of debtor's payment obligation using the bankruptcy estate, shall be null and void by law.

##### Suspension of debt payments

The debtor's suspension of debt payment condition shall not terminate ongoing proceedings or prevent any party to commence new proceedings against the debtor. However, if the claim submitted against the debtor is in respect of the debt that has been acknowledged by the debtor, and the plaintiff does not have an interest in obtaining a judgment to exercise its rights against any third party, after the acknowledgement of such debt, the presiding judges may postpone the decision until the conclusion of the suspension of debt payment process. Also, the debtor cannot be the plaintiff or the defendant in any case concerning rights and obligations related to its estate without prior approval from the administrator.

**Post-filing credit**

- 16** **May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

**Bankruptcy procedures**

The receiver of a bankrupt debtor may obtain an unsecured loan or, with the approval of the supervisory judge, a secured loan.

**Suspension of debt payment procedures**

The debtor together with the administrator may obtain a loan or credit from any third party.

**Set-off and netting**

- 17** **To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

In both bankruptcy and the suspension of debt payments procedures, creditors can set off sums owed by them to the debtor against amounts that the debtor owes to them. However, sums can only be set off in the bankruptcy procedure if one of the following requirements is met:

- the claim and the debt already existed before the declaration of bankruptcy; or
- the claim and the debt exist as a result of transactions carried out with the bankrupt debtor before the bankruptcy was declared.

There is no requirement for the debts to be currently due and payable. However, there is uncertainty about whether or not the receiver (in a bankruptcy) or administrator (in a suspension of debt payments) must approve an intended set-off.

**Sale of assets**

- 18** **In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

**Bankruptcy procedures**

The receiver shall manage the bankruptcy estate and the settlement of the company's debts. The receiver is entitled to sell the debtor's bankruptcy assets by way of public auction according to the applicable law and regulations. If the debtor's asset or property cannot be sold by way of public auction, the sale can be conducted privately with prior approval from the supervisory judge. Secured assets will be sold by the secured creditors through public auction and the proceeds shall be used to pay the secured creditors' claims. The purchaser will acquire the assets free and clear of claim. There is no specific regulation governing 'stalking horse' bids in sale procedures.

**Suspension of debt payments procedures**

The debtor together with the administrator is entitled to sell its assets.

The creditors cannot purchase the debtor's assets and make payment of the purchase price by reducing the amount of its claim against the debtor.

**Intellectual property assets in insolvencies**

- 19** **May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

The IP licensor or owner must continue the debtor's right to use it unless the receiver or administrator confirms the termination of the IP

agreement. Whether or not the IP licence is continued or terminated must also refer to the provisions on the relevant IP licence agreement.

**Personal data in insolvencies**

- 20** **Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

There is no specific provision governing personal data in insolvencies. There is also no general regulation governing the use of personal data in Indonesia. The protection of personal data to a limited degree is regulated for use through electronic media under the Law No. 11 of 2008 concerning Electronic Information and Transaction (the Electronic Information and Transaction Law).

Article 26 of the Electronic Information and Transaction Law stipulates that the use of personal data in electronic media must obtain approval from the person concerned. Any person whose personal data rights on are infringed may file a claim for compensation of damages incurred.

**Rejection and disclaimer of contracts in reorganisations**

- 21** **Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

A debtor undergoing a suspension of debt payments cannot reject or disclaim an unfavourable contract. If the debtor breaches the contract the counterparty may submit a claim for damages.

**Arbitration processes in insolvency cases**

- 22** **How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Bankruptcy and suspension of debt payments proceedings and their related matters cannot be settled by arbitration.

There is no specific provision in the Bankruptcy Law with regard to the continuation of arbitration proceedings after a bankruptcy or suspension of debt payments proceedings is initiated. However, the provision concerning continuation of legal proceedings shall be applicable to the continuation of arbitration proceedings in a bankruptcy or suspension of debt payments. See question 15.

**Successful reorganisations**

- 23** **What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

No specific provision is required to be included in the composition plan. Creditors are classified as preferred, secured and unsecured creditors. In the bankruptcy proceedings the plan must be approved by the unsecured creditors that fulfil a quorum of one-half in number and two-thirds in amount of the total unsecured claims, while in the suspension of debt payments proceedings it must be approved by the unsecured creditors that fulfil a quorum of one-half in number and two-thirds in amount of the total unsecured claims; and the secured creditors that fulfil a quorum of one-half in number and two-thirds in amount of the total secured claims.

The composition plan only described the plan for the debtor to pay its debts, it does not concern the liabilities of officers, directors, advisers and lenders.

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**Expedited reorganisations**


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**24 Do procedures exist for expedited reorganisations?**

There is no procedure for expedited suspension of debt payments under the law, but the debtor and creditors can have a pre-agreed composition plan before the submission of a suspension of debt payments procedure so as to manually expedite the whole suspension of debt payments process.

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**Unsuccessful reorganisations**


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**25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

Proposed reorganisation is defeated if creditors do not agree with the composition plan provided by the debtor, or the presiding of panel of judges of the commercial court does not ratify the agreed composition plan.

If the debtor fails to perform its obligation under the composition plan, the creditor can file a claim for nullification of the composition plan, and consequently the debtor will be declared bankrupt.

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**Insolvency processes**


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**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

During the bankruptcy process there will be several meetings held, namely:

- first creditors' meeting: at the latest, five days after the appointed receiver and the supervisory judge receive the bankruptcy decision, the receiver is obliged to serve a written notice regarding the date and the place of the first creditors' meeting via mail or courier to the known creditors and to put an advertisement regarding the date and the place of the first creditors' meeting in two daily newspapers. At the latest 30 days as of the declaration of the debtor's bankruptcy, a creditors' meeting will be held and chaired by the supervisory judge;
- a verification meeting: at the latest, 14 days as of the declaration of the debtor's bankruptcy, the supervisory judge must issue an order to determine: the time limit for the creditors to file claims; the time limit for the verification of a claim; and the day, date, time and place of the creditors' meeting for verification of claims;
- at the latest, five days after the issuance of the supervisory judge's order, the receiver must serve written notices regarding the order to the known creditors and to put an advertisement in two daily newspapers;
- a meeting to discuss, reject or approve the composition plan submitted by the debtor: after conclusion of claim verification, the creditors will vote to decide on the composition plan; and
- other meetings: the supervisory judge may hold a meeting if it is deemed necessary or requested by: the creditors' committee; or at least five creditors representing one-fifth of the total amount of acknowledged or conditionally approved claims.

Calls for meetings are always done via registered mail or courier service to the known creditors, and advertisement in two daily newspapers having national circulation and local circulation in the domicile of the debtor.

The receiver and administrator shall submit to the supervisory judge its report concerning the condition of bankruptcy estate and the performance of its duties every three months. The report is open for the public.

A creditor may not generally directly pursue the estate's remedies against third parties.

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**Enforcement of estate's rights**


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**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

A creditor may not generally directly pursue the estate's remedies. The receiver may sell the debtor's assets, if it is in the best interests of the debtor and creditors, for the purpose of pursuing the estate's remedies against third parties.

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**Creditor representation**


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**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?****Bankruptcy procedures**

The court may form a temporary creditors' committee consisting of three persons appointed from known creditors in order to provide advice to the receiver. After the conclusion of claim verification, the supervisory judge is obliged to offer the creditors the option of forming a permanent creditors' committee. By request of the unsecured creditors under a resolution approved by majority vote of the unsecured creditors in creditors meeting, the supervisory judge shall: replace the temporary creditors' committee (if a temporary creditors' committee has been appointed before); or form a creditors' committee (if a temporary creditors' committee has never been appointed before).

The creditors' committee is entitled to: provide advice to the receiver; delegate all its rights and responsibilities as creditors' committee to any third party; request the receiver to disclose all books, documents and letters related to the bankruptcy process; request any required information from the receiver; conduct a meeting with the receiver or the supervisory judge; submit to the supervisory judge an objection letter concerning the actions taken by the receiver; request the supervisory judge to order the receiver to conduct certain actions; be present at the inventory of the bankruptcy estate; give approval for the receiver to continue the business of the bankrupt debtor even if a cassation or civil review is filed against the court decision on bankruptcy; and call upon the bankrupt debtor to provide information.

**Suspension of debt payment procedures**

The commercial court must appoint a creditors' committee in the event that: the petition of suspension of debt payment concerns complex debts and involves many creditors; or the appointment of a creditors' committee is requested by creditors representing at least half of the total amount of the acknowledged claims. The administrator, in performing its responsibilities, is obliged to request and consider the suggestion of the creditors' committee.

The Bankruptcy Law is silent on the retention of advisers by the creditors' committee, both in the bankruptcy and suspension of debt payment procedures.

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**Insolvency of corporate groups**


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**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

The Bankruptcy Law does not recognise bankruptcy or suspension of debt payment proceedings of a corporate group. Petition of bankruptcy or suspension of debt payment may only be submitted against an individual or legal person. Bankruptcy or suspension of debt payment proceedings of the parent company will not involve the subsidiaries beyond its share value in the subsidiaries and vice versa. Assets cannot be transferred from an administration in Indonesia to an administration in another country.

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## Appeals

- 30** What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Upon all court orders made by the supervisory judge, appeal may be filed within five days to the commercial court, except for court orders on certain issues as stipulated under article 68, paragraph (2) of the Bankruptcy Law. The right of appeal is automatic, and there is no requirement to post security to proceed with an appeal under Indonesian law.

All court orders in respect of the management and settlement of the bankruptcy estate issued by the presiding panel of judges of the commercial court (eg, court orders on the appointment or termination of receiver, court orders on receiver's fee, etc) cannot be appealed.

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## Claims

- 31** How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

The creditor must submit its claim to the receiver or administrator, including: the detailed calculation or written explanation indicating the nature and the amount of the claim; evidence; and a statement letter stating whether or not the creditor holds any privilege, security right or retention right. The time limit for the creditor filing its claims shall be determined by the supervisory judge. If the claim of a creditor is denied by the receiver or administrator, the creditor can appeal to the supervisory judge. If the supervisory judge cannot settle the dispute, then the dispute must be referred to the district court for examination, with a right to appeal to the High Court and, further, the Supreme Court.

In the event of a transfer of a claim, the voting right owned by the previous creditor shall be transferred to the new creditor. However, the transfer of claim conducted by way of claim splits after the declaration of the debtor's bankruptcy or suspension of debt payment will not create a voting right for the new creditor. Also, as stipulated under article 613 of the Indonesian Civil Code, the creditor shall notify the debtor regarding the transfer of claim. Moreover, it is provided under Bankruptcy Law that any person taking over a creditor's claim before the declaration of bankruptcy or suspension of debt payment may not exercise a set-off right if it can be proven that the said claim was taken over with bad faith and set-off right could not be exercised for any claim taken over after the declaration of bankruptcy or suspension of debt payment.

Claims for contingent or unliquidated amounts are not recognised, given that all claims submitted to the receiver or administrator must be in a definite amount with detailed calculation.

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## Modifying creditors' rights

- 32** May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The court cannot change the rank of the creditor's claim.

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## Priority claims

- 33** Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Apart from employee-related claims, major privileged and priority claims are tax claims, fees of the receiver or administrator, and any costs and expenses incurred in the liquidation of the bankruptcy estate or costs in the suspension of debt payment process, post-bankruptcy financing and lease of the bankrupt's house or offices. All of these preferred claims have to be paid in full from the bankruptcy estate before it is distributed between the creditors.

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## Employment-related liabilities in restructurings

- 34** What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

If the employer is declared bankrupt, it may terminate employment contracts. This triggers the payment of severance packages for the employees. Termination of employment may be performed by giving no less than 45 days' prior notice.

Employee claims for payment of salaries and severance packages are classified as estate claims and must be paid in full from the bankruptcy estate before it is distributed between the creditors. Employee claims for severance packages, although classified as estate claims that must be paid in full from the bankruptcy estate before it is distributed between the creditors, are paid after the enforcement of security right by the secured creditors (see question 44).

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## Pension claims

- 35** What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Since the provision of a pension fund by the employer is not mandatory under the Manpower Law, the pension fund received by the employee will be subject to the terms and conditions of the pension programme conducted by the employer. Generally, in the event of termination of the employment relationship because of a specific reason, the terminated employee shall only be entitled to obtain pension fund calculated until the termination date. In bankruptcy or suspension of debt payment proceedings, the employee may submit its pension-related claim to the receiver. In general, employee claims, including allowances, shall rank as preferred creditors in the bankruptcy proceedings.

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## Environmental problems and liabilities

- 36** In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The debtor is responsible for environmental problems that are subject to criminal sanctions, but if the environmental problem results in a civil claim, the claimant can submit its claim to the receiver.

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## Liabilities that survive insolvency proceedings

- 37** Do any liabilities of a debtor survive an insolvency or a reorganisation?

All of the debtor's liabilities survive the bankruptcy and suspension of debt payment procedures.

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## Distributions

- 38** How and when are distributions made to creditors in liquidations and reorganisations?

The general rule for the distribution of the proceeds of a bankruptcy estate to unsecured creditors is one of equality, subject to the statutory priority rights of certain categories of creditors. The distribution can be made when the estate has become insolvent.

The creditors' ranking is as follows:

- tax claims, whose priority right lasts only five years as of incurrence;
- post-bankruptcy creditors (who have claims on the bankruptcy estate), which are entitled to receive the following payments in full:
  - salary of the receiver;
  - costs in the liquidation of the bankruptcy estate (appraiser's fee, accountant's fee, etc);
  - post-bankruptcy financing;
  - lease of the bankrupt's house or offices; and
  - wages of the employees of the bankrupt company;
- secured creditors; and
- unsecured creditors:

- specific statutorily preferred creditors whose preference relates only to specific assets. Specific statutory preferred creditors prevail over general statutory priority rights;
- general statutory priority rights; and
- non-preferred unsecured creditors.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

A transaction that is entered into within a specific period (one year) before the declaration of its bankruptcy may be nullified by a claim of the receiver by issuing an extrajudicial declaration. If the counterparty refuses to accept the nullification, the receiver must commence proceedings.

Nullification of a transaction made by the debtor may be invoked if the following conditions are met:

- a legal act was performed by the debtor company before it was declared bankrupt; legal acts are acts that are intended to have a legal effect, such as a sale and purchase agreement, a gift or a waiver. Legal acts are either reciprocal (a sale and purchase agreement) or unilateral (a gift or a waiver) in nature;
- the debtor company was not obligated by contract or by law to perform the legal act, or in other words the legal act or transaction was voluntarily conducted by the debtor company. Some examples of transactions voluntarily made are:
  - payment of a debt that is not yet due and payable;
  - granting of security for a debt when the debtor was not obligated to do so;
  - sale of goods by a debtor to his creditor followed by a set-off of the purchase price; and
  - payment of a debt in kind instead of in cash;
- the legal act or transaction prejudiced the creditors' interests; eg, a sale of goods below their fair market value or their disposal as a gift;
- the debtor and the other party in the transaction had knowledge that the legal act or transaction prejudiced the creditors' interests. There is a statutory presumption of knowledge that all transactions performed within one year of a declaration of bankruptcy are prejudicial to the company's creditors by law, provided that it can be established that such a transaction falls into one of the following categories:
  - transactions in which the consideration that the debtor company received was substantially less than the estimated value of the consideration given;
  - payments or granting of security for debts that are not yet due; and
  - transactions entered into by the debtor with certain relatives or related parties of the debtor, or the directors of the debtor company.

The annulment of a payment, even one that is due and payable, is possible in cases where a payment was made to a creditor who knew that a petition for bankruptcy has been registered. The same applies to the payment of a debt based on conspiracy between the company and its creditor with the intention of preferring that creditor over other creditors.

If a transaction is annulled, then the previous condition will be returned as if the transaction had not happened.

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The 'suspect period' to determine whether or not to annul a transaction by a bankrupt debtor is within one year prior to the declaration of the debtor's bankruptcy.

The request of annulment can be submitted by the receiver or by the creditors.

The 'suspect period' is only recognised in bankruptcy.

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### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Directors and commissioners are personally liable for the losses suffered by the company where the company is declared bankrupt and the bankruptcy has been the result of the fault or negligence of such directors or commissioners, and the assets of the company are not sufficient to cover the obligation of the company.

Directors and commissioners of a company that is declared bankrupt are also subject to criminal sanction as follows:

- imprisonment for the maximum of one year and four months, if he or she:
  - has participated in or has given permission to perform actions contrary to the articles of association that cause the whole, or significant part of, losses to the company;
  - with intent to delay the bankruptcy or the judicial settlement of the company, knowing that the bankruptcy or the judicial settlement could not thereby be avoided, has participated or has given his or her permission to borrow money under onerous conditions; or
  - is to be blamed for not fulfilling his or her obligations to maintain the company's books and records or if such books and records cannot be produced in an unaltered condition; and
- imprisonment for the maximum of one year and four months, if he or she fraudulently curtails the rights of the creditors to:
  - forge non-existent expenses, or has not accounted incomes, or has withdrawn any property from the estate;
  - alienate any property, either for nothing or obviously below the value;
  - benefit one of the creditors in the event of bankruptcy or judicial settlement, or at a moment when he or she knew that the bankruptcy or the judicial settlement could not be avoided; and
  - has not fulfilled the obligations in respect of keeping the company's records, and the keeping and producing of books, documents and writings.

Further, directors and commissioners who have been declared guilty in causing a company to be declared bankrupt cannot be appointed as directors or commissioners in other companies within five years as from the date when they were declared guilty.

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### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

A parent corporation, as a company shareholder, is not responsible for the liabilities of its subsidiaries beyond the value of shares that it owns. However, such shareholders' limited liability shall cease to exist, and, therefore, the shareholders shall be personally liable, in the following event:

- the required status of a company as legal entity has not yet been or is not achieved;
- the relevant shareholder, either directly or indirectly, appropriates the company in bad faith for his or her personal benefit;
- the relevant shareholder is complicit in an unlawful act committed by the company; or
- the relevant shareholder, either directly or indirectly, unlawfully capitalises on the company's assets, resulting in the company's assets being rendered insufficient to pay off the debts of the company.

As regards an affiliated corporation, there is no specific provision under the law governing its liabilities for the affiliates.

### Update and trends

Recently there have been several instances where the receiver in bankruptcy proceedings or administrator in a suspension of debt payment process were being 'criminalised' when performing their duties under the Bankruptcy Law. The 'criminalisation' was done by the debtor by submitting criminal complaints to the police to impede the performance of receiver or administrator duties, for example, alleging:

- not allowing or blocking the bankrupt debtor from entering its office or place of domicile, and trespassing on private property under article 167 of the Penal Code;
- falsifying information under article 263 of the Penal Code because of refusing the claim of a creditor that, according to the debtor, is its creditor;

- defamation for publishing a public announcement on the bankruptcy of the debtor; or
- embezzlement given that the receiver or administrator has sold the assets of the bankruptcy estate without the approval of the debtor.

Although, at the end of the day, the allegations were not proven, the investigation processes by the police, including a series of interviews, are seriously impeding the bankruptcy or suspension of debt payment processes.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There is no restriction on claims by insiders or non-arm's length creditors, but it will be the receiver who decides whether or not to recognise the claim or amount of the claim.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

The bankruptcy is the general attachment or seizure of all the debtor's assets. The secured creditors in bankruptcy proceedings may enforce their security right outside the bankruptcy proceedings as if there were no bankruptcy, subject to a stay of 90 days. The stay does not apply to cash collateral and does not affect the right of the creditors to a set-off.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

See questions 9 and 10. Liquidation under the Company Law is conducted upon dissolution of a company. In the company liquidation, all assets are liquidated to pay the creditors' claims.

Under bankruptcy proceedings, the bankrupt debtor can still propose a composition plan, and if approved by the creditors and ratified by the court, the bankruptcy will be lifted, but if the plan is rejected by a creditor or not ratified by the court, the bankruptcy estate is insolvent and the assets will be liquidated.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

##### Bankruptcy procedures

The debtor's bankruptcy shall be concluded if:

- the commercial court judgment on the declaration of bankruptcy is overturned by the Supreme Court in cassation or civil proceedings;
- the declaration of bankruptcy is revoked by the commercial court on the recommendation of the supervisory judge if the bankruptcy estate is not sufficient to pay the bankruptcy cost;
- the debtor, after the declaration of bankruptcy, submits composition plan, the said composition plan is approved by the creditors and ratified by the commercial court, and the commercial court decision ratifying the composition plan has been final and binding; or
- the liquidation of bankruptcy has been completed and all the bankruptcy estate has been distributed to all creditors.

Upon the conclusion of bankruptcy, the debtor is entitled to request the commercial court to rehabilitate the status of the debtor.

### Suspension of debt payment procedures

Suspension of debt payment may be concluded in the event that:

- the composition plan submitted by the debtor is approved by the creditors and ratified by the commercial court, and the commercial court decision ratifying the composition plan has been final and binding; or
- the composition plan submitted by the debtor is rejected by the creditors or not ratified by the commercial court or the debtor fails to implement the composition plan. In this condition, the debtor shall be declared bankrupt.

Notwithstanding the description above, the debtor's suspension of debt payment may be concluded at request of the supervisory judge, one or more creditors, or at the initiative of the commercial court if:

- (i) the debtor, during the suspension of debt payment, manages its assets in bad faith;
- (ii) the debtor causes damage or attempts to cause damages for the creditors;
- (iii) the debtor, without the approval of the administrator, performs a managerial or ownership act over the entire or a part of its assets;
- (iv) the debtor fails to perform its obligation determined by the commercial court when or after the declaration of suspension of debt payment, or fails to perform any actions required by the administrator for the benefit of the debtor's assets;
- (v) the suspension of debt payment can no longer be continued because of the condition of the debtor's assets; or
- (vi) it is impossible for the debtor to fulfil its payment obligation to the creditors within the specified period.

In the occurrence of the conditions in points (i) and (v), the administrator is obliged to submit a petition of conclusion of suspension of debt payment to the commercial court. The commercial court shall hear and examine such petition within 10 days and shall render its decision no longer than 10 days as of the conclusion of the examination process. If the commercial court grants the administrator's petition, the suspension of debt payment shall be concluded and the debtor shall be declared bankrupt.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

The Bankruptcy Law adopts the principle of territoriality. A bankruptcy procedure initiated in another jurisdiction has, in principle, no effect in Indonesia. Assets located in Indonesia belonging to a company that has been declared bankrupt outside Indonesia are not considered part of the bankruptcy estate.

Foreign creditors in liquidation process and suspension of debt payment proceedings are dealt with in the same manner as domestic creditors. The only difference is that the time limit for the submission and verification of claim from foreign creditors shall not apply, if such

domicile of foreign creditors prevents them from reporting themselves beforehand. See also question 8.

Foreign judgment is not recognised in Indonesia.

Indonesia is not a signatory to any treaty on international insolvency or on the recognition of foreign judgments. Furthermore, Indonesia has not adopted the UNCITRAL Model Law on Cross-Border Insolvency.

#### COMI

**48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

The Bankruptcy Law does not recognise cross-border bankruptcy or suspension of debt payment cases. As such, COMI is not applicable in Indonesia.

#### Cross-border cooperation

**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

The Indonesian law system does not provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings.

Courts in Indonesia refused to recognise foreign proceedings or to cooperate with foreign courts because of the territoriality concept.

#### Cross-border insolvency protocols and joint court hearings

**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

The Bankruptcy Law does not recognise cross-border bankruptcy or suspension of debt payment cases. The commercial court does not enter into cross-border bankruptcy or suspension of debt payment protocols or other arrangement to coordinate proceedings with the courts in other countries.



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# Isle of Man

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The legislation applicable to insolvencies and reorganisations is set out in the Companies Act 1931 (the '31 Act), The Companies (Winding Up) Rules 1934 (the Rules) and the Companies Act 2006 (the 2006 Act).

Companies in the Isle of Man can either be incorporated under the '31 Act ('31 companies) or the 2006 Act (2006 companies) and each of the two types of company have different characteristics and statutory powers as governed by and set out in the respective Companies Act.

The '31 Act sets out the statutory insolvency regime for the Isle of Man in conjunction with the Rules.

The '31 Act insolvency regime (ie, sections 155 to 272 (inclusive) and 277 to 280 (inclusive)) is applied to companies incorporated under the 2006 Act by section 182 of the 2006 Act.

One of the circumstances in which a company may be wound up by court as set out in section 162(5) of the '31 Act is if the company is unable to pay its debts.

Section 163(1) sets out the definition of inability to pay debts as:

- (1) *if a creditor, by assignment or otherwise, to whom the company is indebted in a sum exceeding fifty pounds then due, has served on the company, by leaving it at the registered office of the company, a demand under his hand requiring the company to pay the sum so due, and the company has for three weeks thereafter neglected to pay the sum, or to secure or compound for it to the reasonable satisfaction of the creditor; or*
- (2) *if execution or other process issued on a judgment decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or*
- (3) *if it is proved to the satisfaction of the court that the company is unable to pay its debts, and, in determining whether a company is unable to pay its debts, the court shall take into account the contingent and prospective liabilities of the company.*

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The Chancery Division of the High Court of Justice hears all claims to wind up a company for the appointment of a liquidator. Following a judgment of the Chancery Division, a party may appeal a winding-up order to the Staff of Government Division of the High Court of Justice (the Isle of Man Appeal Court Division), and any appeal of that court's decision is to the Privy Council.

Subject to complying with statutory timelines for filing any appeals and complying with the requirements of the Rules in relation to service and advertisement requirements, there are no restrictions on the insolvency matters that the divisions of the courts listed above may deal with.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

No entities are excluded from customary insolvency proceedings as long as they are a creditor and the sum owed by the company is more than £50 and, if the entity is a company, that it has not been dissolved or struck off the register of its county of incorporation. In such a circumstance, the company would have to be restored to the register and be in good standing.

If insolvency proceedings are brought against a protected cell company (PCC) then the creditor can only seek recourse against the assets in the particular cell of which it is a creditor; it cannot proceed or seek recourse against the assets in the other cells of the PCC.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Creditors of a government-owned enterprise can proceed by way of the normal insolvency procedures as set out in this chapter.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No, it has not.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

The principal types of security that can be taken against immovable (real) property in the Isle of Man are in line with those in most common law jurisdictions, namely mortgages, fixed and floating charges and debentures.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

The principal types of security that can be taken against moveable property are liens, pledges (normally share pledges), debentures and title retention.

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## Unsecured credit

### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

All of the Isle of Man insolvency remedies are available to unsecured creditors, and these are in line with other Commonwealth jurisdictions and include: obtaining judgment against the debtor, appointment of a

receiver, arrestment order, charging order and attachment of earnings order. An unsecured creditor can also petition for winding up of a company in the same manner as a secured creditor. None of the procedures are especially difficult or time-consuming and certainly not outside of the normal time for insolvency remedies to be achieved.

No special procedures apply to foreign creditors who can seek recourse against the debtor company in line with the procedures and remedies available to Isle of Man-based creditors.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A debtor company can seek to wind itself up by way of a members' voluntary liquidation (MVL). The steps required for a MVL are set out in the '31 Act.

To proceed with an MVL, the directors of the company (or in the case of a company having more than two directors, the majority of the directors) make a statutory declaration of solvency and the company must pass a special resolution (ie, be passed by members holding more than 75 per cent of the voting shares) that the company be wound up voluntarily.

If the directors of the company are unable to make the statutory declaration then the company must proceed by way of a creditors' voluntary liquidation (CVL).

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Creditors of a company can file a claim for the appointment of a liquidator (ie, an involuntary liquidation) with the Chancery Division. The grounds upon which the court will wind up the company are as set out in question 1, namely:

- if the creditor has served a statutory demand that has not been paid or secured or compounded to the reasonable satisfaction of the creditor within three weeks of service of the demand;
- if the creditor has an unsatisfied judgment against the company; or
- it can prove that the company is unable to pay its debts.

Once the claim is filed (and prior to any liquidator or provisional liquidator being appointed by the court), the company cannot dispose of any of its property, including things in action, transfer any shares or alter the status of the members of the company without the consent of the court by way of a court order.

Further, once the claim is filed, no proceedings can continue or be commenced against the company except by leave of the court.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Isle of Man law does not provide for company voluntary arrangements and administrations. Debtors can, however, use the process set out in both the '31 Act and the 2006 Act for arrangements, mergers and consolidations.

Schemes of arrangement involve a company entering into a compromise or arrangement with its creditors or members, or both. The meaning of compromise or arrangement is wide; the agreement can be about anything that the company and its creditors or members may properly agree.

The scheme must involve a genuine compromise, that is the members or creditors, or both, must obtain some advantage that compensates them for the alteration of their rights.

An application is made to the court for an order directing meetings of the members or different classes of members or the meetings of the creditors or different classes of the creditors (the court meetings), or both, to approve the scheme. In order for the scheme to be approved, a majority in number representing 75 per cent in value of those present and voting, either in person or by proxy, must vote in favour of the scheme.

In the event the scheme is approved at the court meetings, a second and final court hearing is held at which the court will decide whether to

sanction the scheme. Once effective, the scheme is binding on all the creditors and members of each class that approved the scheme.

Similar statutory processes are set out in the legislation for schemes of merger or consolidation.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

As set out at question 11, a creditor can make an application to court for approval of a scheme of arrangement. However, in practice, it is unlikely that it will have sufficient information about the company's financial position to lead a reorganisation.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Isle of Man law does not expressly require a company to commence insolvency proceedings at a fixed time. Directors are under a continuing obligation to consider whether the company is insolvent or likely to become insolvent with no prospect of recovery. At this stage, the directors must act in the best interests of the creditors as a whole.

If the company carries on business whilst insolvent, the directors risk personal liability if, in a winding up, it appears that any business of the company has been carried on with intent to defraud creditors or for any fraudulent purpose.

A liquidator may also consider whether a person who has taken part in the formation or promotion of the company has misapplied or retained or become liable or accountable for any money or property of the company or has been guilty of any misfeasance or breach of trust in relation to the company. If so, the court may order him or her to repay or restore the money or property or pay compensation.

In relation to 2006 companies, directors may also be personally liable to repay the company any distribution that was made to a member where the solvency test was not satisfied immediately after that distribution.

Generally, directors also risk being disqualified in the event they carry on the business of the company in circumstances where it is insolvent.

Unlike under English law, there is no concept of wrongful trading.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

Outside of insolvency, the debtor can continue to carry on business during a reorganisation. It is unlikely to be appropriate to cease to carry on business where the purpose of the reorganisation will be to allow the business to continue in its reorganised form. Relationships will continue under the existing contractual terms (subject to the terms of any scheme), and it is likely that existing and prospective creditors will want more information about the company's financial position and the reorganisation.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

Where a winding-up order is made by the court or a provisional liquidator is appointed, no proceedings can continue or be commenced against the company except by leave of the court.

In respect of a voluntary winding up, there is no restriction on proceedings being continued or commenced. However, the liquidator may make an application to court for a stay on proceedings, for example, on the basis that the issues raised in the proceedings can and should be dealt with in the context of the liquidation as opposed to by way of ordinary civil proceedings.

There is no restriction on proceedings during a reorganisation.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

In a liquidation, a liquidator has the power to raise money on the security of the assets of the company if required. This would be deemed an expense of the liquidator and would therefore have priority over unsecured creditors.

During a reorganisation, the ordinary position in respect of the raising of credit would apply, but it may be that the obtaining of new credit and/or the re-negotiation of existing credit would form part of the terms of the reorganisation itself.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

During a reorganisation outside of insolvency, the usual contractual rules on set-off will apply.

On insolvency, the rules of statutory set off are set out at section 22 of the Bankruptcy Code 1982, which is applied to companies being wound up by section 248 of the '31 Act. The rules provide that on insolvency, where there are mutual dealings between a company and a creditor claiming to prove a debt, the sum due from one party is to be set off against the sum due to the other party.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

A liquidator can (without sanction) sell the real or personal property and things in action of the company by public auction or private contract, including by way of sale of the entire business of the debtor. However, the debtor must beneficially own the property. Therefore, assets subject to a fixed charge or held on trust for a third party cannot be sold.

There are no restrictions on 'stalking horse' bids or credit bidding.

However, in respect of the latter, in a winding up by the court or a CVL, it will be necessary for the liquidator to seek the court's or (if there is one) the committee of inspection's approval as this will amount to a compromise with a creditor. In an MVL, the liquidator would require the sanction of an extraordinary resolution.

In reorganisations outside of insolvency, there are no restrictions, albeit that the court's approval may be required, for example, in a scheme.

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

The debtor's rights to continue using IP on insolvency or the termination thereof will depend upon the terms of the contract as agreed

between the licensor or owner and the debtor. Insolvency will not automatically trigger termination of the rights; however, a specific contract may provide insolvency as a ground for termination. Equally, a liquidator will be bound by the terms agreed with regard to terminating the relevant contract.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The ordinary law on data protection continues to apply despite insolvency, and the legislation contains no special provisions or exemptions.

The company and the liquidator will need to comply with the Data Protection Act and all of the data protection principles, including when entering arrangements such as selling part of the company or its assets. For example, it will be necessary for the liquidator to advise the individuals of the new arrangement and ensure that the transfer is done securely.

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### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

See questions 11 and 14. In reorganisations outside of insolvency, debtor companies do not have the power to reject or disclaim unfavourable contracts, although the rights and obligations of the debtor under contracts may be varied pursuant to the terms of the reorganisation.

In an insolvency, the liquidator has the power to disclaim onerous property including unfavourable contracts.

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### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Arbitration is used very infrequently in Isle of Man insolvencies.

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### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

There are no mandatory requirements in an informal reorganisation; it is a matter for agreement between the creditors.

See question 11.

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### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

There are no provisions for the expedition of reorganisations or schemes or arrangement, and the implementation time will depend on its complexity, although the majority of the time spent on the reorganisation is commonly in negotiation with the creditors and in preparation of the settlement documentation.

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### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

See question 11.

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**Insolvency processes**

**26** During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

**Voluntary winding up**

In the first instance, notices are sent by post to the creditors of the company, calling a meeting to pass the resolution for voluntary winding up. Notice will also be advertised in two local newspapers and in the London Gazette.

During the winding up, the liquidator may call meetings of the creditors at any time it sees fit for the purpose of ascertaining the creditors' wishes.

As soon as the affairs of the company are fully wound up, the liquidator will call a final meeting of the creditors for the purpose of laying an account of the liquidation. Again, such meeting is advertised in two local newspapers and in the London Gazette, specifying the time, place and agenda of the meeting, one month prior to the meeting taking place.

In the event that winding up continues for more than a year, the liquidator must also summon a meeting of the creditors at the end of the first year from the commencement of the winding up, and of each succeeding year, and shall lay before the meetings an account of his acts and dealings and of the conduct of the winding up during the preceding year.

Throughout the winding up, the liquidator should generally keep the creditors up to date on the progress of the winding up. There is no statutory right for creditors to seek access to the books and papers of the company but creditors can apply to the court for an order in respect of the liquidator's conduct of the winding up.

**Winding up by the court**

Unless the court otherwise directs, a meeting of creditors must be held within one month after the date of the winding-up order to confirm the liquidator's appointment and to consider whether to appoint a committee of inspection. Seven days' notice of the meeting must be given and an advertisement must be placed in the London Gazette providing a date and time of the creditors' meeting.

The liquidator has the power to call meetings of the creditors throughout the winding up for the purposes of ascertaining the creditors' wishes.

Notices of the liquidator's intention to declare a dividend and the intention to seek the court's release and dissolution of the company must also be given to creditors.

As for voluntary liquidations, the liquidator should generally keep the creditors up-to-date on the progress of the winding up and must provide reports to the court at regular intervals. Creditors can seek an order from the court requiring the liquidator to provide a creditor with access to the books and papers of the company as it sees fit.

**Proceedings against third parties**

There is no provision under the '31 Act or 2006 Act for a creditor to have the ability to bring proceedings against third parties in relation to losses suffered by the company. However, a liquidator may assign a company's claims to third parties if it is in the interests of the creditors of the company, for example, where the liquidator does not have the funds to pursue the claims.

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**Enforcement of estate's rights**

**27** If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

See question 26.

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**Creditor representation**

**28** What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

See question 26.

The committee of inspection consists of up to five persons (voted by the creditors at the creditors' meeting). The purpose of the committee is to supervise the liquidator, fix the remuneration to be paid to the liquidator or liquidators and modify the powers and duties of the liquidator or liquidators (which can also be modified by the court). The liquidator has to report to the committee on a regular basis. The committee of inspection will also be responsible for determining the process of disposing of the company's books and papers.

No member of the committee, by himself or herself or any employer, partner, clerk, agent or servant may purchase any part of the company's assets, and any such purchase may be set aside by the court.

No member of the committee is, except under and with sanction of the court, directly or indirectly, entitled to derive any profit from any transaction arising out of the winding up or to receive any payment for services rendered by him or her, out of the assets of the company, and/or in connection with the administration of the assets. The court may sanction payment to any member of the committee for services rendered; however the court shall specify the nature of the services and such sanction shall only be given where the service performed is of a special nature.

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**Insolvency of corporate groups**

**29** In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Each member of a corporate group will be treated as a separate entity from any of its members, other than in very specific circumstances. Accordingly, the assets and liabilities of each of the companies are not automatically combined into one pool for distribution in a winding up. However, where there are corporate groups, there may be administrative advantages to having the same liquidator appointed in respect of each of the companies (subject to any conflict); with each entity being treated as its own separate entity.

In a reorganisation of a group of companies, the assets and liabilities of all of the companies can be pooled pursuant to a scheme of arrangement, compromise or consolidation.

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**Appeals**

**30** What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

An appellant has an automatic right to appeal from any order or decision made or given in the matter of the winding up of a company by the court, and such petition must be presented within three weeks after the order or decision complained of has been made, unless such time is extended by the court whose order or decision is appealed from.

There is no requirement under statute requiring security to be posted in order to proceed with an appeal, but the court has the power to order security to be paid.

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## Claims

- 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

The Rules direct that a creditor 'shall ... prove his debt'. The liquidator may impose a time limit in which proofs have to be submitted. Creditors who seek to lodge proof after the expiration of a time limit may do so, but any assets that have already been distributed shall be unaffected; therefore, the creditor runs a risk of missing out on his or her share.

In accordance with the Rules, a debt may be proved by delivering or sending through the post a proof of debt containing or referring to a statement of account showing the particulars of the debt and confirming whether or not the creditor is or is not a secured creditor.

Proof of debts for contingent and unliquidated amounts can be filed in the liquidation. It is for the liquidator to make a determination on the value of the claim, require further particulars in support of the claim and, possibly, reject the claim.

In the event a liquidator rejects a proof of debt, creditors can apply to court to challenge the liquidator's decision within 21 days.

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## Modifying creditors' rights

- 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

The court does not have general jurisdiction to change the priority of creditor's claims, which are determined by statute. However, if the security over the company's assets is not registered at the Isle of Man Companies Registry as in the manner prescribed under the '31 Act and 2006 Act in favour of the creditor, it will be void against the liquidator and any creditor of the company. The prescribed time limit for '31 Companies to file any such charge is within one month of the date of the security/charge being created. There is no time limit for 2006 Companies.

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## Priority claims

- 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

A liquidator will distribute the proceeds of realised assets and pay creditors in a specified order depending on the source of the proceeds, that is, whether they come from a fixed charge, floating charge or uncharged assets. The liquidator's costs, debts to the Crown, employee payments and unpaid pension contributions rank ahead of secured creditors.

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## Employment-related liabilities in restructurings

- 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

In a reorganisation outside of the formal insolvency process, normal rules apply in respect of employment and termination of employment contracts.

Liquidation has no statutory effect on contracts of employment; however a liquidator is likely to terminate employment contracts as part of the winding up and payments due to employees may therein attract priority. Under the Employment Act 2006, where an employer has become insolvent or ceased carrying on business in the Isle of Man, the Treasury may pay certain debts of the employer out of the Manx National Insurance Fund, such as, for example:

- arrears of pay for eight weeks;
- pay during any period of statutory minimum notice;
- arrears for payment for time off;
- an unpaid basic award of compensation for unfair dismissal; and
- up to six weeks' holiday pay accrued in the preceding 12 months.

However, other preferential debts may have priority over these debts.

An employee may claim payment from the Treasury, when a company has ceased business, of an unpaid debt only where he or she has taken all reasonable steps, short of legal action, to recover it from the employer. The employee must make an application in writing to the Treasury within 12 months of the date of termination.

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## Pension claims

- 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Under the Preferential Payments Act 1908, unpaid pension contributions have priority over the debts of ordinary creditors. However, other preferential debts may have priority over unpaid pension contributions in accordance with the Preferential Payments Act 1908.

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## Environmental problems and liabilities

- 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

Manx insolvency legislation does not specifically deal with environmental problems arising prior to or during the course of liquidation. Liability in respect of environmental problems would be found under civil and common law.

While there is no specific reference to the liability of directors or officers for environmental problems within the insolvency legislation, the general rule is that no director, officer, agent or liquidator of a company will be liable for any liability or default of the company unless specifically provided for under the legislation, and except in so far as that person may be liable for their own conduct. Therefore, it would be necessary to consider whether any director or officer of the company could be attributed with any personal liability for their own actions on a case-by-case basis.

Under section 183 of the '31 Act, the liquidator of a company being wound-up by the court has the power to, with the court's permission, bring or defend any action or other legal proceedings that relates to the property of the company; therefore, it would usually be the liquidator who deals with any legal action brought in respect of environmental problems.

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## Liabilities that survive insolvency proceedings

- 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

No. Once a company enters insolvent liquidation, the liquidator will assess that company's liabilities as part of his or her statutory duties to complete the liquidation and the liabilities will be settled as part of the liquidation process.

In a reorganisation of a solvent company, the liabilities may survive depending on the terms of the scheme or other reorganisation.

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## Distributions

- 38 How and when are distributions made to creditors in liquidations and reorganisations?**

In CVLs and MVLs, the liquidator must apply the sale proceeds from the company's assets in satisfaction of its liabilities *pari passu* and then (unless the company's articles of association state otherwise) distribute any outstanding sums to the company's members according to their rights and interests in the company.

In a court-ordered winding up, the liquidator must give the creditors two months' notice of his or her intention to declare a dividend. The notice must specify the date proofs must be received by the liquidator to be considered, and this date cannot be less than 14 days from the date of the notice. Subject to there being no appeals against the dividend, the liquidator can proceed to pay the dividend on the date indicated in the notice.

### Update and trends

There are no pending legislative changes. However, we believe the question as to whether the Isle of Man's insolvency regime ought to be separated from the companies' legislation and stand as a separate piece of legislation may be considered more formally by industry and the government in the future. As set out in this chapter, the Isle of Man High Court has previously assisted foreign courts and insolvency officers, and it is likely that in a world focusing on global cooperation and transparency, the Isle of Man courts are likely to be caused to consider more often how far they can and ought to go in assisting in foreign insolvencies. As the Isle of Man is not a full member of the European Union and its relationship with the EU is limited as set out in Protocol 3, the UK's decision to leave the EU will not directly impact the Isle of Man's insolvency regime and the Isle of Man's recognition of foreign insolvencies.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

Manx company law states that any transactions that are deemed a 'fraudulent preference' may be set aside. In order to demonstrate fraudulent preference, it must be shown that there was an intention to prefer one creditor and that the company was insolvent at the time of the transaction or became so as a result of the same.

A floating charge which is created within six months of the winding up of a company will be invalid unless it is proven that the company was solvent immediately after its creation.

The liquidator can, with the court's leave, disclaim onerous property, such as land burdened with covenants, unprofitable contracts or unsaleable property.

Any dispositions of property or transfers of shares made after the commencement of winding-up proceedings will be void unless the court orders otherwise.

A further catch-all provision to protect creditors is found in the Fraudulent Assignments Act 1736, whereby any fraudulent transfers of assignments of the debtor's goods or effects shall be void and of no effect against just creditors.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

Yes. Floating charges created within six months of the commencement of the winding up of a company are invalid unless it is proven that the company was solvent immediately after the creation of the charge. In terms of a transaction by a debtor which is considered to be 'fraudulent preference' as discussed above, there is no 'suspect period' as the conditions for establishing the offence mean that a sufficient nexus to the insolvency proceedings is inevitable.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Generally no director, officer, agent or liquidator of a company will be liable for any liability or default of the company unless specifically provided for under the legislation, and except in so far as that person may be liable for their own conduct.

However, a director may be held personally liable for his or her company's obligations if it is proven that such director is guilty of fraudulent trading (ie, carried out the business of the company with intent to defraud creditors or for any other fraudulent purpose). An officer of the company may also be held personally liable for misfeasance if during the course of a winding up it appears that such person has misapplied

or retained any money or property of the company. In such case, the liquidator may apply to the court to compel the person to repay or restore the money or property.

While 'wrongful trading' is not recognised in Manx statute, a director could still be liable for wrongful trading under English legislation if company assets were situated in England and Wales.

Directors can be subject to other sanctions during the liquidation process (for example, failure to fully disclose the company's books and records to the liquidator or concealment of the company's property) and may be subject to a fine or imprisonment.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

In Isle of Man law, a company has separate legal personality from its directors and shareholders, and also from other companies in its corporate group. The Isle of Man High Court is very unlikely to make an order that one company be responsible for the debts or obligations of another company in its corporate group, unless:

- such order was requested as part of a scheme of arrangement or compromise arrangement put forward by the company or its creditors; or
- a court decides to 'pierce the corporate veil' because the company in question is a sham, for example, if the company has only one shareholder who is also the sole director.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

No, but it is open to a liquidator to reject a proof of debt filed by a non-arm's length creditor if the liquidator has reasonable grounds to believe that such creditor's claim is not genuine.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

There may be contractual documentation in existence between a debtor and its creditors that allows the creditors to appoint a receiver to take custody of certain of the debtor's property. If no such documentation is in place, if a creditor obtains judgment against a debtor in the Isle of Man High Court of Justice, that creditor may request the coroner (a court officer similar to a bailiff in the UK) to issue 'execution' in respect of that debtor's goods, that is, to seize certain of the debtor's goods as are sufficient to satisfy the judgment debt.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

A solvent company may be liquidated voluntarily (pursuant to an MVL, see above) or dissolved voluntarily by an application made by any director or member of the company. The latter involves an application to the Isle of Man Companies Registry for dissolution where the company is dormant and has no assets or liabilities. It must be accompanied by a statutory declaration by either the director or the member confirming that the company has discharged all its liabilities.

The difference between dissolution and liquidation is that a dissolved company may be restored to the register of companies at any time within 12 years of the date of its dissolution. A liquidated company may not be restored once two years has elapsed since the date the company's name was removed from the register.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

In a winding up by the court, once the liquidator of the company has realised all the company's property, or so much as can, in his or her

opinion, be realised without needlessly protracting the liquidation, and has made a final dividend distribution, then the liquidator must provide a report on the accounts of the liquidation to the court. The court will consider the report, and any objections raised by the creditors or contributories, and either grant or withhold the release of the liquidator accordingly. The court will also make an order that the company be dissolved from the date of the order and the liquidator must report this order to the Companies Registry within 14 days of the date of the order.

In both MVLs and CVLs, as soon as the affairs of the company are fully wound up, the liquidator must prepare accounts of the winding up showing how it has been conducted and that the property of the company has been disposed of. The liquidator must call a general meeting of the company and creditors to show members the accounts and give any explanation as required. The liquidator must give one month's notice of the meeting. Within one week of the meeting, the liquidator must send a copy of the accounts to the Companies Registry and must make a return to the Registry of the meeting held and its date. Once the Companies Registry receives the accounts and the return it will register the same, and on the expiration of three months from the registration the company shall be deemed to be dissolved.

#### International cases

- 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

The Isle of Man courts have demonstrated that they are keen to assist foreign jurisdictions with insolvency proceedings, subject to there being proper scope to do so, if it results in a more efficient and pragmatic approach (see comments of the Isle of Man's First Deemster (Chief Justice) in *Interdevelco v Waste2Energy* (2012) CHP 2012/56 at paragraph 2).

In order to avoid the situation whereby liquidators are appointed in two jurisdictions, it is possible for an application to be made to the Isle of Man courts to recognise the appointment of a liquidator in a foreign jurisdiction and allow the liquidator certain powers over companies or assets, or both, in the Isle of Man.

Foreign creditors in respect of insolvency proceedings in the Isle of Man are dealt with in the same manner as local creditors; all must prove any debts owed to them in the usual course.

The UNCITRAL Model has not been adopted in the Isle of Man, and we are not aware of any considerations for its adoption at present.

#### COMI

- 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

The concept of COMI does not exist in Isle of Man law because the Isle of Man is not a member state of the EU, and, therefore, the directive relating to COMI does not apply on the Isle of Man. From a tax perspective, the question is where the company's 'management and control' takes place.

#### Cross-border cooperation

- 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

The Isle of Man High Court has frequently assisted courts, insolvency officers and others from countries outside the Isle of Man when they have requested assistance in obtaining information and evidence in the Isle of Man especially in cases of alleged wrongdoing or insolvency (see First Deemster Doyle's comments in *Brittain v Impex Services* (2004) CP 2003/96, paragraph 107).

#### Cross-border insolvency protocols and joint court hearings

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

The Isle of Man courts have not to date entered into any cross-border insolvency protocols or coordinating arrangements, or held joint hearings with courts in other countries in cross-border cases.

However, in the case of *Capita v Gulldale* (2014) CHP 2013/145, the Isle of Man High Court ordered that a letter of request could be sent to the English High Court requesting it place the defendant, a Manx company with its centre of main interests in the Isle of Man, into administration under the laws of England and Wales. In the circumstances of the case, the court granted this request, recognising that Manx insolvency legislation does not offer administration, and this would seem the 'efficient and effective' way to deal with the defendant company's assets.



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# Italy

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Italian legislation governing the liquidation, restructuring and insolvency of corporate entities is as follows:

- Royal Decree No. 267 of 16 March 1942 on Insolvency, Composition with Creditors and Compulsory Administrative Liquidation, as subsequently amended and supplemented (the Insolvency Act). Important amendments have been introduced by:
  - Law Decree No. 35 of 14 March 2005 as subsequently converted into Law No. 80 of 14 May 2005;
  - Legislative Decree No. 5 of 9 January 2006;
  - Legislative Decree No. 169 of 12 September 2007; and
  - Law Decree No. 69/2013, as subsequently converted into Law No. 98 of 9 August 2013;
- Law Decree No. 78 of 31 May 2010, as subsequently converted into Law No. 122 of 30 July 2010;
- Law Decree No. 83 of 22 June 2012, as subsequently converted into Law No. 134 of 7 August 2012 (the Development Decree);
- Legislative Decree No. 270 of 8 July 1999, governing the Extraordinary Administration (Law No. 270/1999) as amended and supplemented;
- Law No. 39 of 18 February 2004, governing the Extraordinary Administration of Large Enterprises as subsequently amended and supplemented (Law No. 39/2004);
- the Civil Code (in particular, articles 2272 to 2283, 2308 to 2312, and 2484 to 2496 for the liquidation of partnerships and companies and article 2221 for the insolvency of a commercial activity);
- Legislative Decree No. 385 of 1 September 1993, as subsequently amended and supplemented, which applies where banks and financial institutions are subject to extraordinary administration or compulsory administrative liquidation (the Banking Law);
- Law Decree No. 1 of 5 January 2015, as subsequently converted into Law No. 20 of 4 March 2015, containing urgent provisions for the conduct of companies of national strategic interest in crisis;
- Law Decree No. 83 of 27 June 2015, as subsequently converted into Law No. 132 of 6 August 2015 (Law Decree No. 83/2015);
- European Regulation No. 848 of 20 May 2015 on insolvency proceedings;
- Legislative Decree No. 180 and 181 of 16 November 2015 (Legislative Decrees No. 180/2015 and No. 181/2015), implementing the Bank Recovery and Resolution Directive of 15 May 2014 of the European Parliament and of the Council (Directive 2014/59/EU or Bank Recovery and Resolution Directive);
- Legislative Decree No. 72 of 21 April 2016 (Legislative Decree No. 72/2016), implementing the Mortgage Credit Directive of 4 February 2014 of the European Parliament and of the Council (Directive 2014/17/EU or Mortgage Credit Directive); and
- Law Decree No. 59 of 3 May 2016, as subsequently converted into Law No. 119 of 30 June 2016 (Law Decree No. 59/2016).

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Jurisdiction over insolvency proceedings is vested in the court of first instance located where the company has its principal place of business. Any transfer of the main headquarters of the company during the year preceding the procedure for the declaration of insolvency does not affect jurisdiction. Companies whose registered office is abroad may be declared bankrupt in Italy even if they have not been declared bankrupt abroad (subject to international agreements and EU legislation), and any transfer of the registered office abroad does not preclude Italian jurisdiction if it occurs following the filing of the application for the declaration of bankruptcy by the debtor or any of the creditors, or following the application for bankruptcy by the public prosecutor. In larger regions, the court will have a specific arm dealing with insolvency matters. A supervising judge is appointed by the court and is responsible for the conduct of proceedings and for the supervision of the bankruptcy receiver. The bankruptcy receiver is appointed by the court at the same time as the court makes the declaration of insolvency. Courts cannot appoint a bankruptcy receiver who has either acted as judicial commissioner in a procedure of composition with creditors for the same debtor or joined a professional association with those who have held this position. The bankruptcy receiver must complete his or her obligations within the prescribed deadlines, under penalty of revocation.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Italian insolvency and restructuring proceedings differ from the common law liquidation and bankruptcy procedures in several respects. First, there is no general winding-up procedure for companies. Separate provisions for voluntary liquidation and insolvency are contained in the Civil Code and the Insolvency Act, respectively. It is also a distinctive feature of Italian law that a private individual who is not an entrepreneur cannot be declared bankrupt; therefore (save for the two exceptions listed below) only entrepreneurial entities as defined in the Civil Code are subject to insolvency proceedings. The two exceptions are:

- public entities and other entities (such as banks, insurance companies or other financial institutions) that carry on public services. These are subject to specific insolvency procedures such as compulsory administrative liquidation; and
- entrepreneurs who meet the following requirements:
  - they have made annual capital investments in the business (averaged over the past three years or since the beginning of the activity if less) of an amount of less than €300,000;
  - they have achieved annual gross revenues (averaged over the past three years or since the beginning of the activity if less) for an amount of less than €200,000; and
  - they have an overall amount of (both matured and non-matured) debts of less than €500,000.

The above thresholds may be updated every three years by a decree from the Ministry of Justice. Moreover, there is no declaration of bankruptcy if the overall amount of the outstanding debts stated in the pre-bankruptcy investigation papers is less than €30,000.

The following assets are generally excluded from insolvency proceedings or exempt from claims of creditors:

- items and rights of a strictly personal nature;
- maintenance, salary, pension, pay cheques and anything that the entrepreneur earns from his or her business that is required to maintain the entrepreneur and his or her family (relevant thresholds are set by the supervising judge, taking into account the personal conditions of the entrepreneur and of his or her family);
- proceeds deriving from the legal use of his or her children's assets, assets that are part of a trust fund and revenues arising therefrom; and
- items that cannot be seized by law (such as religious items, clothes, bedding, beds, dining tables, cupboards).

The insolvency proceedings also include assets that are acquired by the debtor during the proceedings, less liabilities incurred for the purchase and maintenance of the assets themselves. However, with the authorisation of the creditors' committee, the receiver may refuse to accept assets that are acquired during the insolvency proceedings if the cost required to purchase and maintain them exceeds their value.

As a general principle, creditors may not bring individual (interim or enforcement) actions in relation to assets included in the insolvency proceedings once insolvency has been declared, even in relation to debts accrued during the insolvency proceedings.

Small gifts from, and acts of, the debtor resulting from a moral duty or for purposes of public utility are excluded from claw-back actions even if they took place in the two years prior to the insolvency declaration, provided that the donation is proportionate to the donor's assets.

#### Public enterprises

#### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Article 2221 of the Italian Civil Code and article 1 of the Insolvency Act exempt 'public entities' from bankruptcy, but do not exclude companies (although held by public agencies) that actually carry out a business from bankruptcy declaration. Despite this, a significant body of case law (among others: Court of Naples, 31 October 2012 and 24 October 2012; Court of Appeal of Genoa, 2 February 2012; Court of Catania, 26 March 2010) has recently stated that said companies, under certain conditions, could also qualify as 'public entities' and, thus, benefit from the exemption from bankruptcy. This case law trend is based on the principle of substance over form: a business carrying out an essential public service should meet the test of 'public entity', regardless of that fact that it is, in form, a business organisation. This interpretation is challenged by another branch of case law (Court of Appeal of Naples, 27 May 2013, 24 April 2013 and 15 July 2009) and also by the Supreme Court of Cassation (27 September 2013, No. 22209). The ruling of the Supreme Court is based on various grounds, among which: (i) the principle of substance over form is contrary to the general rule set out in article 4 of Law No. 70/1975, according to which 'any new public entity can be incorporated or acknowledged only by operation of law'; (ii) companies providing essential public services are subject to the extraordinary administration procedure of large enterprises, under specific provisions intended to ensure continuity of services – a system exempting such entities from bankruptcy but not from extraordinary administration would be unsound. The foregoing must, however, be considered in light of further recent case law (among others: Court of Nola, 30 January 2014; Court of Naples, 9 January 2014; Court of Verona, 19 December 2013) according to which the specific category of 'in house' companies should be exempted from bankruptcy. This case law tries to tie in with principles on jurisdiction for liability actions against corporate bodies of 'in-house' companies (Court of Cassation, 25 November 2013, No. 26283 and 10 March 2014, No. 5491). The Courts of Palermo and Reggio Emilia confirmed, however, that even in-house companies can be declared bankrupt if not all conditions for exemption are strictly met.

#### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

As regards banking crises, Legislative Decrees No. 180/2015 and No. 181/2015 implemented the Bank Recovery and Resolution Directive by amending the Banking Law and identifying the Bank of Italy as the relevant national resolution authority.

Banks operating in Italy are required to prepare a full recovery plan that sets out the measures to be taken by those institutions for the restoration of their financial position following a significant deterioration. This will provide the resolution authority with the appropriate information to plan how the institutions' or groups' essential functions may be isolated and continued. Resolution authorities are also to be provided with powers to require an organisation to take steps to restore financial soundness or to reorganise its business.

Using the recovery plan as a basis, the resolution authority will prepare, after having consulted the European Central Bank (for those banks on which supervision is carried out jointly by the Bank of Italy and the European Central Bank), a resolution plan for each institution, setting out different options for resolving the institution in a variety of scenarios.

When an institution is failing, a resolution authority should have a harmonised minimum set of resolution tools, including:

- a sale of business tool: enabling authorities to effect a sale of part or the whole of the business without shareholder consent;
- a bridge institution tool: providing for a new institution to continue to provide essential financial services to clients of the failed institution;
- an asset-separation tool: enabling the transfer of 'bad' assets to a separate vehicle or 'bad bank'; and
- a bail-in tool: ensuring that most unsecured creditors of an institution bear appropriate losses.

Resolution powers are triggered when the competent authority, on the basis of objective tests specified by the law, determines that the institution is failing or likely to fail and there are no alternative measures that would prevent such a failure within a reasonable time frame. The resolution is chosen when the Bank of Italy verifies the existence of the public interest, namely, when the resolution is necessary and proportionate to reach one or more of the resolution objectives and the winding up of the institution under compulsory administrative liquidation would not meet those resolution objectives to the same extent. The choice of the specific resolution tool to adopt rests with the competent authority.

Other special rules on banking crises and crises of financial institutions also residually apply when the recovery and resolution procedures cannot be undertaken. These rules are set out by the Banking Law (for banks and banking groups) and the Financial Consolidated Act (for other intermediaries) apply, which provide for different proceedings depending on the seriousness of the crisis, to be assessed in light of the amount of capital losses and of the irregularities or violations of the legislative and administrative applicable rules.

If it is possible for the company to survive, the Minister for the Economy and Finance may place the company into special administration following such a proposal from the Bank of Italy. The Bank of Italy will subsequently appoint various special bodies to provisionally manage the company and, most importantly, to assess its financial situation and propose solutions in order to ensure the protection of savings.

In an urgent situation, if the conditions for placing the bank into special administration have been met, the Bank of Italy can appoint a commissioner to manage the bank for a maximum of two months (temporary management).

If the crisis is irreversible and cannot be overcome, the company will undergo a compulsory administrative liquidation ordered by the Minister for the Economy and Finance on the Bank of Italy's proposal. The Bank of Italy will appoint the liquidating bodies, which will act under its supervision.

No other regimes apart from the special administration and compulsory administrative liquidation described above are provided for large institutions, regardless of the size of the insolvent company.

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**Secured lending and credit (immoveables)**


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**6 What principal types of security are taken on immoveable (real) property?**

Under Italian law, loans are mainly secured by way of a mortgage over immoveables. Some types of immoveables (aircraft, vessels and motor vehicles) are subject to specific regimes applicable to the constitution, validity and enforcement of a mortgage over that type of asset.

A mortgage grants the right to appropriate the asset (even against third-party transferees) and a priority on the proceeds of the sale of the mortgaged assets.

There are three types of mortgage over immoveables:

- legal mortgage: provided for by law (eg, for the benefit of transfer of a real estate property, a security for the performance of the transferee's obligations under a transaction);
- judicial mortgage: whenever a judgment is entered against a debtor on the debtor's personal property; and
- conventional mortgage: whenever the parties agree to grant a mortgage, for example, as security for a loan. A mortgage over immoveables may only be validly constituted by notarial deed.

Mortgages are established through the registration of a mortgage deed in the property register of the place where the property is located, or in the relevant register for registered chattels. The mortgage deed must clearly identify the mortgaged property and state the exact value of the obligations secured.

Legislative Decree No. 72/2016, implementing the Mortgage Credit Directive, introduced a new contractual mechanism to ensure the enforceability of security granted by consumers to financial institutions or intermediaries in the context of:

- loans backed by mortgages over residential immoveable property; and
- loans granted for the purchase or conservation of land or buildings either existing or projected.

The Decree gives the parties the right to include a clause in the credit agreement stating that failure by the client to repay 18 monthly instalments will cause the transfer of the immoveable over which security is given (or of the proceeds of its sale) to the creditor. In any case, if the value of the collateral is higher than the amount of the existing debt, the consumer has the right to receive the exceeding amount. At the time of the conclusion of the credit agreement, the parties may also agree, by specific clause, that the transfer of the goods may extinguish the debt even if the immoveable is worth less than the outstanding debt.

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**Secured lending and credit (moveables)**


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**7 What principal types of security are taken on moveable (personal) property?**
**Pledge**

The main type of security taken over moveable property is the pledge. A pledge may be taken over any moveable property, including shares (whether listed or unlisted), patents, trademarks, businesses, book debts or bonds owned either by the debtor itself or by a third party to secure the debtor's obligations.

By executing the pledge, the pledgor transfers possession of the pledged asset to the pledgee or to a jointly appointed custodian. Possession is retained by the pledgee or the custodian until the obligations secured by the pledge have been discharged in full. Failing performance of the secured obligation, the pledged asset may be sold. Where the court consents the pledged asset may also be assigned to the pledgee in discharge of the claim.

It is essential to prove that the pledge is created in writing on a date certain at law in order to enforce the pledge against third parties or to gain priority in insolvency proceedings. The Civil Code sets out specific rules governing how the date is determined.

In the past, there has been academic debate and conflicting case law regarding the constitution and enforceability of pledges over listed shares, bonds and other financial instruments. It was not clear whether a pledge over financial instruments deposited at Monte Titoli (the Italian clearing system) or, more generally, a pledge over instruments, which could be substituted with similar instruments in kind and value, was valid and enforceable. The 1998 reforms of the financial markets

and case law developments have however confirmed that such pledges are validly constituted.

**Non-possessory pledge**

Law Decree No. 59/2016 introduced *pegno mobiliare non possessorio*, a new form of security over moveable assets available to businesses aimed at improving businesses' access to lending and boosting growth.

Any business registered in the Companies' Register is now allowed to grant a pledge over its assets to a broad range of creditors, without losing the right to use and/or trade the assets (in contrast to what would happen for ordinary Italian pledges). Furthermore, any proceeds from the use and/or disposal of pledged assets shall automatically be subject to the same form of security without additional formalities.

In the past, under Italian law the only security interest that allowed the security giver to dispose of the secured assets was the special lien under the Italian Banking Act (see below). However, the special lien is only available to banks as a security for medium-long term loans and qualified investors as a security for medium-long term bonds. By contrast, the newly introduced non-possessory pledge can be granted to any type of creditor as a guarantee for any obligation (including those arising from short-term credit lines and future obligations related to the pursuit of the business activity, as long as they are determined or determinable and the maximum amount is indicated).

The agreement must be in writing and the pledge may be created over existing and/or future assets, to the extent they are used for the conduct of business and are sufficiently described (a general reference to a category of assets or to a total amount would suffice).

This new security must be registered with a new online register held by the Italian Tax Revenue Office and is enforceable vis-à-vis third parties as from the date of registration.

In the context of insolvency proceedings, non-possessory pledges may be enforced by the creditor only after his or her credit is admitted to the statement of liabilities as a preferential credit. The new security interest is subject to the claw-back provisions applicable to ordinary pledges.

**General or special liens**

Liens (both special and general) are granted by law to certain creditors.

A general lien is created upon all moveable assets of the debtor. A special lien is created over specific moveable or immoveable assets.

With a few exceptions the granting of a lien is neither dependent on the parties' agreement nor on public notification.

Liens allow the creditor to satisfy his claim in priority to other creditors, although in compliance with the rank expressly set out by law (as described below).

General liens may not be exercised if exercising the lien would prejudice third parties who have rights over the moveables concerned (except where the moveable assets have been seized by a creditor).

Special liens on moveable property may, however, be executed in priority to rights acquired by third parties over the assets concerned. Where a pledge and a special lien have been created over the same asset the pledge takes priority and the creditor with a special lien cannot enforce the lien in priority to the pledge.

**Special lien under article 46 of the Banking Law**

Article 46 of the Banking Law provides for a special lien created with the agreement of the parties.

The special lien is a security that may be created voluntarily on unregistered moveables (such as equipment and licences) by a company as security for medium or long-term banking loans. The main characteristic of this security is that the creation of the special lien does not require transfer of possession of the relevant asset but only a written deed.

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**Unsecured credit**


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**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

Any unsecured creditor may, before the debtor becomes insolvent, initiate individual proceedings to enforce his rights. If certain conditions are met, a creditor may obtain a summary judgment that is

immediately enforceable and may subsequently obtain an attachment order over the debtor's assets. Unsecured creditors need to participate in the insolvency or bankruptcy proceedings to enforce their rights. A request to participate must be submitted to the judge supervising the proceedings before any distribution plan is approved. Unsecured creditors' claims will rank senior to any unsecured claim submitted after the approval of the distribution plan. Where the debtor has already been declared insolvent, unsecured creditors simply file their request to participate in the insolvency proceedings and any individual proceedings commenced before such declaration lose their effect.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Stock corporations and limited liability companies may be voluntarily dissolved by passing a resolution in the shareholders' general meeting, on any one of the events set out below.

The events are as follows:

- expiry of the company's fixed duration as stated in the by-laws;
- achievement of (or the impossibility of achieving) the purpose for which the company was established;
- if the shareholders' meeting can no longer function or remains inactive;
- if the capital is reduced to less than the legal minimum and the shareholders have not provided for any increase;
- if there are no profits or reserves available to pay a withdrawing shareholder, and if it is impossible to reimburse the holding of the withdrawing shareholder; or
- for any other reason laid down in the by-laws.

If any of the above events occur the directors of the company may not undertake any new activity or enter into any new business. If they do so, they will be jointly and severally liable for the debts arising thereafter. A company in voluntary liquidation may still become insolvent in which case the company's directors have a duty to file a request for a declaration of insolvency.

The provisions of the Development Decree envisage that in the period running from the date on which the petition for a composition with creditors (or for the validation of a restructuring agreement: see question 11) is filed until the court validates such composition or agreement, the rules that require the company to be wound up where its corporate capital is reduced below the statutory level, as specified above, do not apply.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Article 5 of the Insolvency Act states that a commercial entrepreneur may be deemed insolvent when, owing to default or other circumstances, the entrepreneur is unable to pay its debts as they fall due. Normally a situation of transitional illiquidity or financial difficulty that is likely to be cured in the short term would neither compel the debtor nor give grounds to creditors for filing insolvency proceedings.

The proceedings are initiated by a judgment of the competent court rendered upon a petition filed by one or more creditors, by the debtor, or by the public prosecutor. In practice petitions are normally filed by one or more creditors.

The effects of the court making a declaration of insolvency are:

- the debtor is deprived of its business and assets, including all those assets received during the bankruptcy procedure, and is no longer entitled to manage them, unless the court expressly authorises the temporary continuation of trading (which rarely happens);
- commencement of bankruptcy proceedings results in an immediate suspension of the payments of all debts and liabilities of the debtor (all the acts, transactions, payments (made or received by the insolvent debtor) and formalities with third parties that have been carried out after the declaration of bankruptcy are not effective as regards the creditors of the debtor);
- certain payments made, securities given or transactions entered into by the debtor in a certain period before the debtor's submission to a judicial liquidation procedure (varying from six months

to two years) can be set aside and clawed back if certain conditions are met;

- legal actions commenced by creditors, including uncompleted enforcement proceedings, are stayed and any execution or attachment on the assets of the insolvent debtor cannot be further pursued (save for some enforcement proceedings relating to certain mortgage loans that are subject to specific Italian registration); and
- any monetary obligation of the debtor towards each claiming creditor must be verified during the insolvency procedure.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The main types of reorganisation and liquidation procedure are:

- composition with creditors;
- debt restructuring agreement;
- extraordinary administration; and
- extraordinary administration of large enterprises.

The requirements for a debtor to commence a financial reorganisation are different in relation to each of the proceedings mentioned above.

#### Composition with creditors

A debtor in 'crisis' (see below) may file a petition for a composition with its creditors with the local court. Also creditors, who represent at least the 10 per cent in value of the total debt, can file a concurrent petition for a composition with creditors. As a general rule, the petition must contain a proposal for an agreement with creditors and must be accompanied by a restructuring plan, a report of an expert assessing the plan's feasibility, and other documents illustrating the debtor's financial situation. The expert has to be an independent professional, appointed by the debtor, entered in the register of auditors who can be either a lawyer, a business consultant, an accountant or a professional partnership (but, in the case of a partnership, partners have to meet the professional requirements of the aforementioned practitioners). It is not a requirement for the debtor to be technically insolvent at the time of filing the proposal, it is sufficient that the debtor is in a state of 'crisis' (a situation of temporary illiquidity or financial difficulties). The debtor's proposal may provide for a wide range of arrangements, including, for instance, the assignment of assets or the attribution of shares or financial instruments to creditors (as a means of satisfying their claims) and the division of creditors into different classes, each of which may be offered different treatment. The petition is subject to the approval of the majority of the creditors representing the majority of the credits admitted to vote. If the petition provides for different classes of creditors, it will be approved if it is approved by the majority of the creditors (by value) admitted to vote in the majority of the classes. In this case, the Insolvency Act provides that the court (at the request of an opposing creditor and not ex officio) may approve the petition despite the rejection of the plan by one or more classes of creditors, if the terms of the petition allow the creditors that voted against it to be satisfied to the same extent as they would have been following a practicable alternative procedure (ie, the dissenting creditors are 'crammed down').

The debtor's proposal can provide that secured creditors are not fully repaid, provided that the secured creditor obtains at least the market value of the secured asset (this market value being the market value that could have been achieved in a liquidation sale) and does not receive worse treatment than unsecured creditors, to whom, in any case, the debtor's proposal has to guarantee the payment of at least 20 per cent of the unsecured debt. Should the proposal provide for part satisfaction of the secured creditors' claims, they will be admitted to vote for the portion of the claim that has not been satisfied. Secured creditors are also admitted to vote (notwithstanding that the debtor's proposal provides for their full satisfaction) if they waive their security.

Pursuant to the Development Decree, the debtor may also file a 'conditional' petition for a composition with its creditors, (ie, a generic petition without the restructuring plan and the other documents generally required by law), reserving its right to file a definitive proposal, plan and other documents within a certain period, which the court will set at between 60 and 120 days (with the possibility of a further extension of 60 days: see article 161 of the Insolvency Act). Within this period, the debtor may change strategy and opt to file a petition for the validation

of a debt-restructuring agreement instead of filing the definitive petition for a composition with creditors.

Law Decree No. 69 of 21 June 2013, as subsequently converted into Law No. 98 of August 2013, amended certain aspects of the 'pre-composition' with creditors to prevent abuse and provides for the following:

- the debtor must deposit a list of its creditors (indicating the amount of the respective credits), together with its financial statements, when requesting to open the procedure;
- the court has the power to reduce the period to between two and six months after the initial request to deposit the remaining documentation if the debtor's activity results in it not being suitable to continue the procedure;
- the court has the power to appoint a judicial officer to monitor the debtor's management and report any breaches to the court during the procedure (such as the concealment of losses); and
- the debtor must provide reports to the court at least once a month during the procedure (it is up to the court to decide what information must be provided). Law Decree No. 83/2015 provides that the petition for a composition with creditors may also be filed by creditors in cases where the debtor's petition does not provide for the satisfaction of at least 25 per cent of unsecured creditors and as long as it is an approved proposal. The petition for a composition with creditors, whether complete or 'conditional', is published in the Companies' Register and once published:
  - creditors may not start or continue any enforcement or interim actions on the debtor's assets, nor may they acquire preferential rights (unless authorised by the court), on penalty of nullity;
  - any mortgages registered in the 90 days prior to the publication of the petition in the Companies' Register will have no effect on creditors;
  - each creditor is obliged to set off debit and credit balances with the debtor (provided that the debts arose before the submission of the petition for the composition with creditors);
  - interest ceases to accrue on creditors' claims;
  - until the order allowing the composition is issued, the debtor may carry out acts of ordinary administration and, where authorised by the court, urgent acts of extraordinary administration; and
  - the debtor may ask the court to authorise the termination or the suspension of ongoing contracts (excluding employment contracts): in this case, the other party has a claim in damages equal to the damages caused by the failure to comply with the contractual provisions.

Once the petition has been declared admissible, the court appoints an officer who monitors the directors of the company.

A composition that has been approved by a court is binding on all creditors existing before the publication of the relevant petition in the Companies' Register. However, creditors keep their rights as regards any joint obligors, and the debtor's guarantors. During the sale of assets, offers for the purchase of goods can be made not only by the debtor, but also by third parties, provided that their proposals are approved and comparable.

### Restructuring agreements

Alternatively, the debtor may ask the court to validate a debt restructuring agreement executed with creditors that represent at least 60 per cent of the debtor's outstanding debts or with 75 per cent of the financial creditors representing at least 50 per cent of the debtor's outstanding debts and without prejudice to the full payment of non-financial creditors. To do so, it must file the same documentation required for the composition petition (see above), together with an expert's report attesting: the accuracy of the company's data, the feasibility of the agreement and whether the creditors not party to the agreement will be paid in full. According to the Development Decree, such suitability will have to be verified by an expert based on specific indications established by law.

The agreement is published in the Companies' Register and for 60 days from the date of the publication creditors may not start or continue any enforcement or interim actions on the debtor's assets, nor may they acquire preferential rights, unless other creditors agree.

The debtor may also request a prohibition on interim or enforcement actions during the negotiations on the agreement.

### Extraordinary administration

Extraordinary administration is available to companies that: employed at least 200 employees during the previous year (including those admitted to the redundancy fund), have debts equalling at least two-thirds of their assets and are insolvent but able to show serious restructuring prospects within strict time limits (to be achieved through the sale of business assets, financial restructuring or assignment of contracts).

The court is tasked with assessing the chances of achieving such restructuring. After hearing the advice of the judicial commissioner and the Ministry of Economic Development concerning the opening of the extraordinary administration procedure, the court issues a decree that places the company under the administration procedure or, if the restructuring is judged as not achievable, the court will make a bankruptcy order. The Ministry of Economic Development appoints one or three commissioners, who are primarily responsible for drafting a 'plan of reorganisation' specifying the assets to be kept as well as those to be transferred, and any possible trade structures. The execution of the plan must be authorised by the Ministry of Economic Development after hearing from a supervisory committee (which is a consultative body) appointed by the Ministry.

The main effect of the procedure is that the commissioners are only responsible for the liquidation of the company or the transfer of the company as a going concern to a purchaser, as the case may be.

### Extraordinary administration of large enterprises

In response to the Parmalat collapse the Italian government amended the procedure of extraordinary administration. The amendments were intended to facilitate and expedite the restructuring and reorganisation of large insolvent companies. In the past, the economic and financial restructuring provisions set out by the extraordinary administration procedure have been little used – the preferred route being a break-up and disposal of the company's assets.

The extraordinary administration of large enterprises is available to insolvent companies with least 500 employees and an overall debt of €300 million.

The extraordinary administration of large enterprises is a procedure whereby a company is admitted to extraordinary administration and a special commissioner is appointed. The Ministry of Economic Development can admit large enterprises to extraordinary administration and appoint a special commissioner immediately upon application by the insolvent company. The court is informed of the company's application and the Ministry's decision. For companies providing public services the Prime Minister or the Ministry of Economic Development shall appoint the commissioner and may fix the conditions of the appointment, even in derogation of the applicable provisions.

The role of special commissioner can be performed by a single individual who shall:

- within 60 days of appointment (which can be extended by an additional 60 days), file with the competent court a report on the state of insolvency and the viability of the restructuring and extraordinary administration (on the basis of which the court shall declare the insolvency and adopt the ensuing measures);
- within 180 days of appointment (which can be extended by an additional 90 days), file with the Ministry of Economic Development (which has the power to approve) the following:
  - a plan for the economic and financial restructuring and reorganisation of the company or disposal of business assets for a period not exceeding two years (restructuring plan); and
  - a detailed report of the reasons underlying the insolvency of the company or the group;
- until the plan is authorised, the commissioner may request authorisation to implement those transactions (or categories of transactions) that are necessary to ensure the continuation of the business and protect the economic and commercial value of the group. Such authorisation is not required for any transaction implemented in the ordinary course of business or having a value (when considered individually) lower than €250,000; and
- if the Ministry of Economic Development does not approve the restructuring plan within 60 days from the rejection of the plan,

the company must evaluate whether it could be suitable to file an alternative plan relating to the disposal of business assets.

Should the ministry reject the plan, the competent court shall, upon hearing the commissioner, make a bankruptcy order and open judicial liquidation proceedings.

As an alternative to the procedure above, the commissioner may carry out a private negotiation for the disposal of the business concerns and assets if the purchaser guarantees to provide such public services for a certain time and complies with the relevant legal provisions. The commissioner's decision shall comply with the principles of transparency and non-discrimination governing any insolvency and restructuring procedure and the price for the dismissal shall not fall below the market value (as estimated by the Ministry of Economic Development).

Any merger transaction carried out according to the restructuring plan approved by the Ministry of Economic Development is deemed to reflect the general public interests and does not require further governmental approvals provided that it is not an abuse of a dominant position and does not have the effect of restricting competition. For six months from its admission to the restructuring procedure, the company must still comply with any legal requirements for the possession of a licence or concession necessary for the exercise of its corporate activity. If parts of the business that require a licence or concession are sold, such licences and concessions are transferred to the purchaser.

If the commissioner is willing to dispose of certain business assets to protect the economic and commercial value of the group, the commissioner and the purchaser shall enter into a consultation procedure with the unions to agree on the transfer of the employees; in particular, the commissioner and the purchaser may agree to transfer only some of the employment contracts granting the possibility for employees to benefit from the redundancy fund. Any decision relating to the employee redundancy or, unemployment, will be agreed among the parties in a very short time frame, enabled by the extraordinary administration procedure of large enterprises which halves the time periods under the applicable employment laws.

In summary, the extraordinary administration of large enterprises is different to the extraordinary administration procedure in three key respects:

- it provides that the two stages are merged into one with a sole commissioner having all powers, so that the reorganisation may be pursued in a shorter time frame;
- it enhances the powers of the ministry as regards those of the court, with the former having most approval powers; and
- the commissioner may at any time apply for the avoidance of earlier detrimental corporate transactions.

The extraordinary commissioner may (within 60 days of appointment) ask the Ministry of Economic Development to extend the extraordinary administration of large enterprises to any other group company.

Finally, according to Law Decree No. 1/2015, converted into Law No. 20/2015, companies that manage at least one industrial site of strategic national interest, such as the steel-making plants of Ilva, will benefit from the extraordinary administration procedure for companies operating in essential public service sectors. In such cases, certain exceptions to the extraordinary administration procedure for companies operating in essential public service sectors apply. These include, in particular:

- if the company is already under extraordinary receivership, the application to be admitted to the procedure can be submitted by the extraordinary commissioner, who can be appointed as special commissioner in the new procedure by the Ministry of Economic Development;
- for companies providing public services and companies managing at least one industrial site of strategic national interest, the special commissioner may carry out a private negotiation not only to sell, but also to rent business concerns and assets. In such cases, and with exclusive regard to business concerns and assets included in the negotiation, the special commissioner is not required to file any of the following: (i) the aforementioned restructuring plan with the Ministry of Economic Development; (ii) the detailed report of the reasons underlying the insolvency of the company or the group with the Ministry of Economic Development; and (iii) a report on

the state of insolvency and the viability of the restructuring and extraordinary administration with the competent court; and

- for 18 months (and not six, as is provided for other companies) from its admission to the restructuring procedure, any company providing public services or managing at least one industrial site of strategic national interest must still comply with any legal requirements for the possession of a licence or concession necessary for the exercise of its corporate activity. If parts of the business that require a licence or concession are sold, such licences and concessions are transferred to the purchaser.

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## Involuntary reorganisations

### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Only the extraordinary administration (as opposed to extraordinary administration of large enterprises) can be commenced by one or more creditors filing a petition. On receipt of the petition, the court, after consultation with the competent administrative authorities, initiates a procedure that:

- declares the debtor insolvent;
- appoints one or three commissioners; and
- suspends all legal proceedings commenced by creditors against the debtor.

Once insolvency has been declared and the relevant procedure has commenced, creditors or third parties may file a proposal for a composition with the court, with the aim of closing the insolvency proceedings with a reorganisation agreement with its creditors. Such agreement may envisage a restructuring of the company's debts, including through the sale of assets or other transactions. The debtor (or any company in which it has a holding or which is subject to joint control) may only file a petition a composition with creditors one year after the declaration of insolvency and within two years of the decree that enforces the final schedule of liabilities.

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## Mandatory commencement of insolvency proceedings

### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Insolvency proceedings are commenced by a judgment following a petition filed by the debtor, its creditors or a public prosecutor. When a company is insolvent or near insolvency, its directors are under a duty to avoid preferential payments and not worsen the financial position of the company. In particular, should the share capital of a company fall below the prescribed minimum threshold and the company ceases to have the statutory minimum net asset value, the directors are under a duty not to enter into new transactions and are obliged either to increase the capital or to resolve to voluntarily liquidate the company.

Breach of these duties may result in criminal liability and in personal civil liability for the loss suffered by the company (see question 41).

Transactions carried out by an insolvent company before the declaration of insolvency may be subject to a clawback action in the event they fall within the cases provided by the Insolvency Act and the Civil Code. A director who has carried out transactions falling under articles 216 and 217 of the Insolvency Act (fraudulent or simply bankruptcy) can be charged with criminal liability.

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## Doing business in reorganisations

### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

The conditions under which the debtor may carry on business during a reorganisation (and the role of the courts involved) vary according to

the type of procedure, as outlined in question 11. As a general rule, in a composition with creditors, the debtor is permitted to continue trading only to the extent necessary to carry out or complete particular transactions, and thereafter only under the direction of the supervising judge and the day-to-day supervision of the commissioner. Transactions other than those in the ordinary course of business (for example, any new loans, disposals of real estate, etc) may only be made with the written consent of the supervising judge. Any third-party debts arising from such acts have priority status.

The Development Decree has introduced particular rules for compositions that are intended to facilitate the continuation of the business activities, and may be implemented by selling the business as a going concern or by transferring it to another company. The same possibility is also granted to debtors filing petitions for the validation of debt restructuring agreements.

In order to carry out a composition that continues the debtor's business, the debtor must file a plan indicating the expected costs and earnings arising from the continuation of the business, the resources required and the coverage procedures. A coverage procedure is a plan showing how to meet the financial needs of the composition with creditors. In particular, it explains which are the financial resources required to enable the continuation of the activity. The plan must consider among the 'costs' the financial burdens and the eventual reimbursement of principal until the sale of the company to third parties, or, if the company is not sold, until the creditors have been satisfied. The plan must also be accompanied by an expert's report certifying that continuing the business will serve to ensure the best interests of the creditors. It is also possible to provide for a moratorium (for up to one year from the validation of the composition) covering the payment of preferential creditors (with pledges, liens or mortgages).

The debtor may also ask the court to: authorise it to take out loans with priority status (if an expert certifies that they are in the best interests of the creditors) and authorise the payment of previous debts for the provision of goods or services (if an expert states that such services are essential for the continuity of the business and are in the best interests of the company's creditors). The court may also authorise the debtor to take out loans with priority status when a 'conditional' petition for a composition with creditors has been filed and on an urgent basis without an expert's certification, once having heard from the main creditors. The same authorisation (to pay debts due for the provision of goods or services) may also be requested by debtors filing petitions for the validation of debt-restructuring agreements.

The activities carried on by the debtor during a composition with creditors (following its validation) are generally supervised by the supervising judge, the receiver and the creditors' committee who verify the company's compliance with the procedures established in the validation decree.

In both extraordinary administration and extraordinary administration of large enterprises, the ministerial decree that initiates the procedure will normally permit the company to continue its business for various reasons (including the need to protect employees' interests), whereas contracts such as leases, supply contracts or contracts that have already been executed by one of the parties are subject to the same conditions as set out in the Insolvency Act for the other insolvency procedures (ie, they may be terminated at the commissioner's or liquidator's discretion). During extraordinary administration of large enterprises, authorisations, certifications, licences, concessions and other acts or securities are to be transferred to the tenant or the purchaser in the case of the letting or sale respectively of companies and branches of companies. Furthermore, the commissioner must require the tenant or purchaser of plants to file, when submitting the offer, a business and financial plan covering investments (indicating the necessary financial resources and coverage) and outlining the strategic objectives of the group companies' production.

Following the declaration of bankruptcy the directors lose all powers of administration save for:

- the power to appeal against the declaration of the company's insolvency or other court decrees or both;
- the power to bring an action in certain circumstances against the bankruptcy receiver or the creditors' committee; and
- the power to apply to court to suspend a sale of the company's assets.

In addition, the directors will be entitled to receive a copy of the bankruptcy receiver's report and are able to bring claims in respect of this report.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

From the date on which the insolvency was declared, no legal action can be started or continued against the insolvent party's assets and any legal proceedings that are commenced or continued are void.

There are exceptions to the prohibition in relation to tax and land credit procedures where the insolvent company is in compulsory administrative liquidation.

In a composition procedure enforcement and interim actions are blocked from the date on which the petition is published in the Companies' Registry and any judicial mortgages registered in the 90 days prior to the filing of the petition are ineffective. The same prohibition on creditors starting or continuing any legal action against the insolvent party's assets also operates where an early 'conditional' petition for a composition is filed (ie, a generic petition without a restructuring plan and the other documents required (see question 11)).

Similarly, the Insolvency Act provides that, in the case of petitions for the validation of a debt restructuring agreement, within 60 days of the agreement being published in the Companies' Register creditors are prohibited from bringing interim or enforcement actions in relation to the debtor's assets and cannot obtain priority rights, unless such rights are agreed by the other creditors.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

A debtor may not manage or dispose of its assets if declared insolvent. Any transaction or payment made or received by the debtor after the declaration of insolvency is ineffective against the creditor, who is obliged to return to the insolvent estate any sums so acquired.

This principle does not apply to a composition with creditors where the debtor is not dispossessed of its assets and continues to manage its assets under the judicial commissioner's supervision.

As mentioned above (see question 11), under the Development Decree, debts arising from loans entered into as part of a composition with creditors (or validated debt restructuring agreement) have priority status.

Similarly, this provision also applies to debts arising from loans issued for the purposes of filing the petition for composition (or for validation of the debt restructuring agreements) where such loans were envisaged in the plan (or in the restructuring agreement) and the priority status is envisaged in the decree with which the court approves the petition. Moreover when the debtor files its petition for composition with creditors (or for the validation of a restructuring agreement), it may ask the court for authorisation to take out loans with priority status. In making such a request an expert must confirm that taking out the loans would be in the best interests of the company's creditors. The authorisation may also regard loans that are only identified by type and amount, even if they have not yet been the subject of negotiations.

Finally, the court may also authorise the debtor to grant pledges or mortgages to secure such loans.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Creditors have a right to set off debts they owe to the debtor against claims that they have against the debtor, even though they have not expired before the declaration of insolvency.

Set-off will not take place where the creditor purchased a claim that remains unexpired after the declaration of insolvency or in the one-year period immediately prior to the declaration.

A prerequisite for the right to set-off is that the debt and credit to be set-off against each other are liquid or may be made liquid promptly and easily and are of the same nature.

The principles of set-off apply to all insolvency procedures.

### Sale of assets

**18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

There are different procedures for the sale of the debtor's immoveable or moveable assets: an auction sale of immoveable assets to protect creditors' interests in bankruptcy proceedings and a private sale for moveable assets and assignment of claims. The procedures are subject to the supervision of the court and in some cases to the (non-binding) opinion of the creditors' committee.

In order to speed up the sale procedure and to guarantee the best realisable value, payment by instalments can be granted to the purchaser. Moreover, the judge can identify and utilise the best methods to determine price, publicity and award criteria for the most economically advantageous tender. The judge will order the sale by auction when, according to his evaluation, the auction price of the assets could exceed half of their market value. The judge can authorise the purchaser to pay in instalments. In this case, if asked by the purchaser, the judge can also authorise his possession of the assets. An independent, irrevocable and on demand guarantee has to be issued by a bank, an insurance company or a financial intermediary.

The transfer of a business as a going concern (or a branch thereof) implies the transfer of all those assets that are organised for the purpose of carrying out that business or that branch of the business (including real property, plants and machinery, stocks, trade receivables goodwill and contracts (including employment contracts)).

If a transaction qualifies as a transfer of business as a going concern, certain provisions of the law concerning contracts, employment, liabilities and receivables pertaining to the business become applicable. While the parties may agree to derogate from such laws in many respects they will be unable to derogate from the law in relation to certain rights of third parties (ie, employees and creditors).

The transferor remains liable to the creditors after the transfer of the business for the debts that exist at the time of the transfer, unless the creditors have given their consent to the transfer. The transferee is jointly liable along with the transferor for the debts and liabilities of the business, if and to the extent such debts and liabilities are recorded in the accounts of the transferor.

In general terms, this rule is aimed at protecting the creditors' interest, and cannot be derogated by the parties. However, according to case law the parties may contractually exclude the debts and liabilities from the transfer of the business, with the stipulation that such exclusion shall be effective only between the parties and not as regards the creditors.

The Insolvency Act and Law No. 270/1999 provide for specific rules on the matter, according to which:

- unless agreed otherwise, the transferee of a business as a going concern is not liable for the of the business debts arising before the transfer; and
- the bankruptcy receiver or commissioner may provide for the transfer of the business as a going concern or assets or receivables by way of contribution to one or more companies, with the exclusion of liability on the transferor for the liabilities arising from the carrying out of the business prior to the transfer.

According to Law No. 270/1999, the sale of a business as a going concern (or part thereof) or the sale of a group of assets of the insolvent company is made in accordance with specific provisions, pursuant to which, inter alia:

- the transferee must undertake to continue the same business activity for at least two years;
- the transferee must maintain the employment level established at the time of the transfer for at least two years. Insofar as the

employees are concerned in the framework of the trade unions' consultations applicable in the of transfer the of business as a going concern (the consultations), the commissioner, purchaser and employees' representatives may agree on certain exceptions to Italian law on the protection of employees transferred by way of a transfer of business as a going concern (TUPE legislation);

- in the framework of the consultations, or after the unsuccessful conclusion of the consultation, the commissioner and the transferee may agree to transfer only parts of the businesses as a going concern with the identification of the employees in those parts of the business to be transferred to the transferee;
- the commissioner may also proceed with a disposal of assets and liabilities initiated by the insolvent company, with the exclusion of the transferor from the liabilities related to the exercise of the business prior to the disposal; and
- the existing liens and guarantees in favour of the transferor maintain their validity and rank in favour of the transferee.

Certain Italian employment provisions setting out a favourable and protective regime for employees in the event of any transfer of business concerns shall not apply to any transaction under this procedure. In particular, a derogation is made to the application of article 2112 of the Italian Civil Code, which provides that employees retain any rights arising from the employment relationship with the transferor, including the terms and conditions of the employment, and any dismissal following the transfer shall be deemed wrongful.

Likewise, under the Development Decree it is also possible to derogate from article 2112 of the Italian Civil Code where the transfer relates to a business for which a composition with creditors has commenced or a debt restructuring agreement has been validated, provided that an agreement has been reached regarding the maintenance of employment levels.

The application of the principle of the automatic transfer from the transferor to the transferee of all the employees of the business can be excluded by the transferor and transferee under certain conditions. This procedure must involve a consultation with the trade unions.

Once a sale agreement has been agreed the sale can be 'suspended' every time a better irrevocable offer is presented to the bankruptcy receiver although such an offer must be higher than the original offer by at least 10 per cent. The power of the bankruptcy receiver to suspend the sale is discretionary and the bankruptcy receiver will have to assess the reliability of the offer to ensure that it has not been presented to hinder the regular sale procedure.

As regards credit bidding, although there are no provisions on the point, on the basis of general principles such offsetting does not seem to be possible because while the creditor's claim is against the bankrupt, the debt accrued by the purchase of the asset would be against the mass of creditors. Thus, since the bankrupt and the mass of creditors are separate entities, compensation in such a situation would breach the principle of *par condicio creditorum*.

Regarding the composition procedure the Development Decree has introduced specific rules where the composition requires the sale of the business concern or the contribution of the business concern to one or more companies (including newly incorporated companies) – known as composition with continuity of the business. In such cases, the plan filed by the debtor with the court may also envisage the sale of any assets that are not required for the company to operate and:

- the ancillary documentation for the petition for composition must describe the costs and proceeds expected from the continuation of the business, as well as the financial resources and the relevant coverage procedures; and
- the debtor must submit an expert report that certifies the continuation of the business is in the best interests of the creditors.

Finally, the rules on a composition with continuity of the business provide that contracts pending on the date on which the petition is filed may not be terminated as a result of the start of proceedings.

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**Intellectual property assets in insolvencies**
**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

Contractual clauses (either in the IP field or otherwise) that provide for the termination of a contract if either party is declared insolvent are ineffective. If an IP contract has not yet been executed (in full) when either party is declared insolvent, the execution of the IP contract is suspended until the bankruptcy receiver, after the authorisation of the committee of creditors, either accepts to continue of the contract on behalf of the insolvent debtor (assuming all the rights and obligations thereto), or resolves to terminate the contract. Furthermore, the counterparty can solicit the choice of the bankruptcy receiver, requesting the court to set a deadline of 60 days for such decision and on expiry of the deadline the contract is deemed to terminate.

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**Personal data in insolvencies**
**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

The lawful use of customer data in the context of insolvency proceedings is not restricted, unless there is a change in the entity in charge of data processing or in the one that owns such data. The lawfulness of the use of customer data is assessed against the provisions of Legislative Decree No. 196 of 30 June 2003 (Legislative Decree No. 196/2003) and must be in line with the specific use for which the customers provided their consent.

In the event any such change occurs, including in case of transfer of the insolvent company to a purchaser, if the data transferred fall under certain sensitive categories identified in article 37 of Legislative Decree No. 196/2003 (eg, among others, data processed by using electronic means aimed at defining the profile or the personality, or at analysing habits or consumer choices, or at monitoring the use of electronic communications services, with the exception of technically indispensable processing to provide services to users), it is necessary to carry out some notifications related to the change in the entity that owns and manages customer data:

- before the end of the data processing, the assignor has to notify the Italian Data Protection Authority of the end of the processing and the change of the data controller; and
- before beginning the data processing, the purchaser must notify the Italian Data Protection Authority that it will take on the processing.

In any event, customers must be notified of all necessary information to be able to identify the entity or individual who owns and is in charge of the processing of their personal data. Hence, in the case of purchase of the business of the insolvent company or acquisition of the company itself it will then be necessary to inform customers that a different entity is holding their personal data. The means through which such notice is effectively given are to be determined from time to time. The Italian Data Protection Authority issued instructions for specific circumstances of transfer of data in order to simplify the process when one-by-one communications are not feasible (eg, in the event of transfer of entire business units in the banking sector).

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**Rejection and disclaimer of contracts in reorganisations**
**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**
**Composition with creditors**

The debtor may request the court (while submitting a petition for a composition with creditors, or afterwards, once the order allowing the composition procedure has been issued) to authorise it to terminate

pending contracts or suspend them for no more than 60 days (which may only be extended once). The contract counterparty is entitled to damages, equal to the damages that would have arisen from default: this sum will be paid not with priority, but in the same way as any other debts in accordance with the rules on the priority of claims. However, such rules do not apply to employment contracts, property lease contracts or, under certain conditions, preliminary residential property sale contracts.

There are particular rules for composition with continuity of business: in this case, any contracts pending on the date on which the petition is filed are not terminated as a result of the commencement of the procedure, even if they have been executed with the public administration, and any stipulation to the contrary will be null and void.

**Bankruptcy and compulsory administrative liquidation**

In bankruptcy and compulsory administrative liquidation procedures the general rule is that if an agreement has not yet been performed or has not been completely performed by both parties when one of the parties is declared bankrupt, the performance of the agreement shall, unless otherwise provided by law, be suspended until such time as the bankruptcy receiver, having been authorised by the creditors' committee, declares that he is exercising his right of subrogation and replaces the bankrupt party as party to the agreement, thereby assuming all the obligations thereunder, or that he is terminating the agreement. The contract counterparty may give the bankruptcy receiver formal notice and ask the supervising judge to set a deadline of no more than 60 days to make such a decision. If such deadline expires and no action is taken by the bankruptcy receiver, the agreement is deemed to terminate.

If the agreement is terminated, the contract counterparty is entitled to submit a creditor's claim relating to the failure to perform the agreement, but is not entitled to claim compensation for damages.

Any action for termination of the agreement brought prior to the bankruptcy against the defaulting party will take effect in respect of the bankruptcy receiver.

Contractual clauses that provide that bankruptcy constitutes a ground for termination are invalid. However, this rule does not apply to certain contracts, which are deemed terminated by law as a consequence of the commencement of any procedure.

**Extraordinary administrative procedures**

In extraordinary administrative procedures, the extraordinary commissioner may terminate any agreement, including contracts requiring a continuous or periodical performance that have not yet been performed or have not been completely performed by both parties on the date on which the extraordinary administration process starts. Until such time as the right of termination is exercised, the agreement will continue to be in existence.

Once the execution of the restructuring plan has been authorised, the contract counterparty may give the extraordinary commissioner 30 days' notice in which to elect to continue the contract; once such period has expired, the agreement is deemed to be terminated. Again, the general rule does not apply to employment agreements, or real property lease agreements where the extraordinary commissioner shall replace the lessor, unless agreed otherwise.

If the bankruptcy receiver elects to adopt the contract and then breaches its terms the contract counterparty has a damages claim that ranks with a higher priority than unsecured creditors but behind secured creditors. Payment of such damages – if not challenged – must however be authorised by the creditors' committee or by the court.

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**Arbitration processes in insolvency cases**
**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

In a composition with creditors, the company may only enter into arbitration with the prior written authorisation of the supervising judge. In compulsory administrative liquidation, the liquidator may enter into arbitration, but if the claim is of indeterminate value or exceeds

€1,032.91, it has to be authorised by the administrative body supervising the liquidation, which will do so having consulted the supervisory committee.

Arbitration, however, is rarely used in insolvency proceedings.

In insolvency proceedings, the court will allow arbitration to continue after an insolvency case is opened, but if the agreement containing an arbitration clause is terminated, the pending arbitration proceedings cannot proceed. In the event that the bankruptcy receiver replaces the debtor as a party to the agreement, the capacity to sue and be sued is transferred to the bankruptcy receiver, with the prior authorisation of the supervising judge: thus, the bankruptcy receiver is bound by the arbitration agreement. Moreover, in this case, once the arbitration panel has been informed of the insolvency, it must notify – or ask the non-insolvent party to notify – the bankruptcy receiver that a proceeding is pending, and once notification has been served and the bankruptcy receiver has been informed, the arbitral award may be enforced against the company.

All claims arising from bankruptcy proceedings must only be submitted to the court that declared the bankruptcy, which is the sole court with jurisdiction. Notwithstanding this rule, according to academics and case law, certain claims may be submitted to arbitration; in particular, claims against third parties and aimed at ‘restoring’ the estate of the insolvent company – which are not strictly connected to the bankruptcy proceedings – can be referred to arbitration, such as compensation or damages claims or claims aimed at obtaining repayment of a debt.

Note, however, that arbitration is not available for claims relating directly to the insolvency such as the collection or distribution of assets, claims against orders or other judgments issued by both the court and the supervising judge, ‘late’ creditors’ claims (which have not been filed within the time limit set by the court) or any other claim aimed at challenging the assessment of the liabilities made by the supervising judge. Finally, it is still controversial whether clawback claims may be submitted to arbitration. It is worth noting that, according to Italian academics, if the bankruptcy receiver decides to carry on a contract (of the insolvent company) that includes an arbitration clause, such clause remains effective with regard to the insolvency procedure and the receiver is not entitled to avoid its effects.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

A company may propose a composition with creditors if it is ‘insolvent’ or in crisis.

In a composition with creditors, the company may propose a debt restructuring and satisfaction of creditors’ claims by any means, including:

- by way of a transfer of assets, or other transactions to creditors or a company controlled by the creditors; and
- the issuance of shares, quotas or bonds to creditors or a company controlled by creditors or of other financial instruments or debentures.

One of the main features of the composition with creditors is that once the tribunal has admitted the company to the procedure, all creditors with claims prior to the date of the admission must suspend their actions until the final approval of the tribunal. The composition with creditors must be approved, on a vote, by creditors representing the majority by value of all ‘admitted’ claims. Note that creditors who do not take part in the relevant meeting may submit their disagreement by telegram, letter, fax or e-mail. Failing that, they are regarded as consenting and taken into account to calculate the majority.

After the creditor vote the composition must also be approved by the tribunal. The tribunal may only refuse its approval if it believes the composition has not complied with all legal requirements.

As part of the composition the company may propose:

- the division of creditors into classes according to their legal status and homogenous economic interests. The latter must be assessed in relation to the specific proposed plan. Factors such as the type of credit, its amount, the time of its formation or its maturity as well as whether there is a possibility of satisfaction and the existence of

- guarantees will be relevant to determine whether economic interests are sufficiently similar economical claims; and
- different treatment of creditors of different classes.

Where there is more than one class of creditors, each class must vote separately. The petition will be approved if it the majority of classes vote in favour. However, the Insolvency Act provides for the possibility of cram down in that the tribunal may approve the petition notwithstanding that one or more classes of creditors voted against it, if the terms of the petition allows the dissenting creditors to be satisfied to the same extent as they would have been following a practical alternative procedure.

The debtor’s proposal can provide that secured creditors will not be fully satisfied, provided that they obtain at least the value of the secured asset that could have been obtained in a liquidation sale and they do not receive worse treatment than the unsecured creditors.

Should the proposal provide for the partial satisfaction of the secured creditors’ claims, the affected secured creditors will be admitted to vote on the petition in respect of the portion of his claim that remains unsatisfied. Secured creditors are also admitted to vote if they waive (all or parts of) their security (notwithstanding the fact that the debtor’s proposal provides for the full satisfaction of their secured claim).

Furthermore, acts, payments and securities entered into or given pursuant to a composition with creditors (provided that the composition with creditors obtains the final approval by the court) are not subject to clawback actions.

Debt-restructuring agreements may also have wide-ranging contents and provide for various ways in which to restructure the company’s debts.

However, in order to obtain the court’s validation, this type of agreement has to involve creditors that represent at least 60 per cent of the debts, and the petition must be filed together with a report by an expert (see question 11) (chosen by the debtor), that attests to the accuracy of the data and the feasibility of the agreement, with particular regard to whether it is suitable to ensure full payment of third-party creditors within 120 days of the validation (in the case of debts outstanding on that date) or within 120 days of the expiry date (in the case of debts not outstanding on the date of the validation).

As with compositions with creditors, where such agreements are validated by the court, the relevant payments are immune from any clawback actions (in the event of bankruptcy).

The same principles are also applicable to the extraordinary administration of large enterprises. In the case of extraordinary administration, the Ministry for Economic Development may, on the basis of the opinion by the extraordinary commissioner and having heard the supervisory committee, authorise the insolvent entrepreneur or a third party to propose an arrangement to the court. The court will then decide on the arrangement proposal.

The reorganisation plan is binding only on creditors who have entered into it and cannot create releases in favour of third parties.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

An insolvent debtor may try to avoid formal insolvency proceedings by an out-of-court settlement or a rescheduling agreement with creditors. These arrangements, between the debtor and all or some of its creditors (very often with lenders), are not subject to court endorsement and do not bind those creditors who do not expressly enter into the arrangement. While such procedures are more flexible and quicker than traditional voluntary reorganisations, these arrangements may result in possible criminal liability if they fail and result in the collapse of the company.

Along with these informal pre-packaged reorganisations, two forms of expedited reorganisations have been recently introduced in the framework of composition with creditors procedure.

The first concerns agreements for the restructuring of debts in which the debtor submits to the court a voluntary settlement agreement for the restructuring of its debt that it has previously entered into with creditors representing at least 60 per cent by value of total claims (which may also include tax claims). The debtor also files with the court a report by an expert attesting that the agreement ensures the satisfaction in full of the debts of those creditors who are not a party to

the agreement within 120 days of the validation (in the case of debts outstanding on that date) or within 120 days of the expiry date (in the case of debts not outstanding on the date of the validation). The agreement is published in the Companies' Register and is effective from the date of publishing. For the 60 days following the publication date, the creditors cannot initiate or start interim or enforcement actions against the debtor's assets or acquire priority rights, unless agreed with other creditors. The creditors and any other interested party may challenge the agreement within 30 days of its publication. The agreement is binding only for those creditors that entered into it.

The debtor may request for a ban on commencing or continuing injunction or enforcement proceedings prior to 60 days from the publication of the agreement in the Companies' Register (subject to making certain filings).

During the negotiation of the agreement the debtor may change strategy and file a petition for a composition with creditors, without prejudice to the effects (such as the suspension of enforcement and interim actions) arising from the petition for the validation of the restructuring agreement.

Any payments and securities carried out or granted in execution of an agreement for the restructuring of debts approved by the court are expressly excluded from clawback actions (see question 40).

The Insolvency Act also provides for another form of reorganisation: extrajudicial composition. These agreements are not subject to clawback actions provided they are implemented as part of a plan that is likely to allow the reconstruction of the debt of the company and to ensure the company's financial situation is redressed.

Furthermore:

- (i) term loans in any form granted in the implementation of a composition with creditors or an agreement of debt restructuring may be paid in advance;
- (ii) term loans for the purpose of presenting the request of admission to the composition with creditors or the request of approval of the agreement on debt restructuring may be paid in advance if the composition plan or the agreement allows term loans and as long as the advanced payment has expressly been provided by the tribunal decision accepting the request for admission to the composition with creditors or approving the agreement on debt restructuring;
- (iii) these rules also apply to term loans made by shareholders, for up to 80 per cent of their amount; and
- (iv) sums owed to any person in charge of drafting the report, may be paid in advance as long as the advance payment has expressly been provided by the tribunal decision accepting the request for admission to the composition with creditors or approving the agreement on debt restructuring and is attached to the motion admitted to the composition with creditors.

With reference to claims in points (ii), (iii) and (iv), such creditors are excluded from voting and from being considered part of the majority for the approval of the composition and from the computation of the credit percentages for the purposes of the agreement on debt restructuring.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A petition for composition with creditors will be declared inadmissible if the statutory requirements for admission have not been met. The court will issue an unchallengeable decree declaring the petition to be inadmissible once it has heard the debtor. A declaration of insolvency and commencement of insolvency proceedings, may only be issued at the request of one or more creditors, or the public prosecutor, provided that it has been verified that the debtor is insolvent and that the other statutory requirements for the declaration of insolvency have been met.

The same rules apply where the composition has not been approved by the creditors or when, following the approval of the composition it is no longer judged to be feasible the judicial commissioner will inform the creditors and the court will follow the same process as if the plan was declared inadmissible.

Authorisation of the composition with creditors may also be revoked ex officio by the court (which will inform the public prosecutor and the creditors), where it becomes apparent the debtor has hidden any part of its assets, wilfully omitted to declare one or more debts,

declared non-existent liabilities or committed other fraudulent acts. At the end of the proceedings, the court issues a decree and, at the request of the creditor or the public prosecutor, may declare the company insolvent if the relevant requirements are met. The same rules apply if, during the composition proceedings, the debtor carries out unauthorised acts or acts intended to defraud the creditors.

Finally, any creditor may ask for the composition to be terminated if the debtor fails to comply with the arrangements for the composition (within the year following the composition's deadline). However, the composition may not be terminated for a minor default.

If a reorganisation plan is not approved by the creditors and a judicial liquidation order is granted by the court, the debtor may prevent insolvency if, for example, it still has available funds provided by a third party. The same result is achieved if the debtor fails to satisfy the conditions set out in the creditors' resolution.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The bankruptcy receiver will give creditors notice of the insolvency order by registered post, which will also indicate the date of the hearing to verify the existence of their claims. Following the verification hearing the bankruptcy receiver prepares a partition plan. Creditors whose claims have been partially admitted or rejected will be notified by the bankruptcy receiver by registered post or any other form of communication where receipt can be evidenced. Creditors are allowed to challenge the bankruptcy receiver's partition plan within 15 days from notification. Such challenge is filed against the bankruptcy receiver and all other creditors whose partition quote may vary should the challenge be successful. Within 30 days of the bankruptcy judgment, the committee of creditors must be appointed by the court. Such committee has a general supervisory and consultative role, and may authorise the bankruptcy receiver's actions or express an opinion on the conditions provided under the law. Furthermore, under certain conditions, the creditors' committee can also ask the court to replace the bankruptcy receiver. However, there is no express provision authorising the release of liabilities owed by third parties who are not part of the debtor group through a reorganisation plan.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

There are no procedures by which the creditors can pursue the estate's remedies if the insolvency administrator is without assets to pursue a claim.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

A creditors' committee may be formed as a corporate body appointed by the judge and composed of a limited number of creditors.

After 2006, the powers of such committees have been increased: they have become both an active stakeholder as well as an essential co-operator with the bankruptcy receiver during bankruptcy procedures.

The creditors' committee has a central role in authorising the bankruptcy receiver's actions and in controlling the bankruptcy management carried out by the bankruptcy receiver.

## Insolvency of corporate groups

### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Usually in the insolvency of a corporate group, the procedures of extraordinary administration and extraordinary administration of large enterprises apply.

When a company is subject to the extraordinary administration procedure as part of a corporate group, the procedure extends to the other insolvent companies in the group. Although the procedure is the same, the individual proceedings are separate and the companies' assets are not pooled. Each company maintains their financial autonomy and each insolvent company is only liable for its own obligations. A list of creditors will therefore be drawn up for each company in the group before the court can declare such company to be insolvent. The costs of the extraordinary administration are borne by the individual companies of the group in proportion to their respective assets.

If a company is subject to an extraordinary administration of large enterprises and is part of a group of companies, the extraordinary commissioner may ask the Minister for Economic Development to admit other insolvent companies in the group to the procedure by submitting an application for insolvency to the relevant court. The proceedings for each group company may be implemented jointly with those for the parent company or separately.

If the restructuring programme provides for implementation through a composition, several group companies subject to the procedure of extraordinary administration may submit a single proposal, subject to the autonomy of their respective assets and liabilities. Such autonomy may lead to differentiated treatment, even within the same class of creditors, according to the financial situation of each individual company to which the composition proposal refers.

Where an insolvent company has offices in various EU member states the competent court for the insolvency proceedings shall be where that company's group carries out its main operational decisions (as ascertainable by third parties). Therefore, jurisdiction tends to lie with the country in which the main interests of the parent company are located, on the presumption that, although the subsidiary conducts its business in other member states, in practice it merely receives and follows the strategy of the parent company.

## Appeals

### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

The decree of enforceability of the statement of liabilities issued in the context of insolvency proceedings may be appealed by way of:

- opposition to the statement of liabilities;
- appeal against the credits admitted to the statement of liabilities; and
- revocation of credits or rights admitted or excluded.

A specific procedure is established that applies to any of these three kinds of appeal. The opposition to the statement of liabilities may be brought by: any creditor and anyone having any rights on moveable or immoveable property excluded by the statement of liabilities. It is aimed at opposing the denial or partial acceptance of the request of admission to the statement of enforceable liabilities. The opposition is brought against the bankruptcy receiver.

The appeal against credits admitted to the statement of liabilities may be brought by:

- any creditor;
- anyone having any right on moveable or immoveable property owned or possessed by the individual or entity undergoing insolvency proceedings; and
- the bankruptcy receiver.

It is aimed at appealing the acceptance of a request of admission of a concurring creditor. The appeal is brought against the concurring creditor, whose application has been accepted.

The revocation of credits or rights admitted or excluded may be brought by:

- the bankruptcy receiver;
- any creditor; and
- anyone having any rights on moveable or immoveable property either admitted or excluded from the statement of liabilities.

It is aimed at the annulment of the orders issued in the context of the appraisal of the liabilities, after the expiry of the time limits to bring the above-mentioned opposition and appeal, when the acceptance or the rejection of claims is deemed invalid by reason of:

- forgery, wilful misconduct or mistake that induced the court to make a mistake on a relevant fact; or
- lack of knowledge of a relevant document that was not produced in a timely manner for reasons not depending on the appealing party.

The revocation is brought against the concurring creditor, whose application has been accepted, or against the bankruptcy receiver, when the application was rejected.

The appellants listed above have an automatic right of appeal. They do not need to seek any permission before bringing the appeal.

Finally, no bond shall be posted in order to proceed with an appeal, but obviously the normal court fees required to begin a new proceedings have to be paid by the appellant.

## Claims

### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

After the declaration of insolvency, a notice is sent to all creditors specifying the date by which their claims must be lodged (which is normally about two months after the order and before the hearing for the preparation of the creditors' list). If any creditor considers that it is entitled to any security by way of, for example, a mortgage or lien, the creditor must inform the bankruptcy receiver within the time specified in the notice. There is no statutory form for the claim but it should nevertheless state the name and address of the creditor, the amount due and attach any supporting documentation.

A claim may be submitted after the hearing for the preparation of the creditors' list but the creditor may be asked to support the costs of arranging a further hearing. Any creditor whose claims have not been recognised or have been partially recognised may lodge a challenge to the decision within 30 days of the hearing. Within the same time period, any creditor may challenge the recognition of other creditors' claims.

The Italian Bankruptcy Act does not formally regulate the transfer of claims already admitted to bankruptcy proceedings. However, Italian case law suggests that transfer is possible but the new creditor has to file the claim again in order for it to be recognised, as final admission implies an assessment of the claim with respect to a specific claimant, whose identity is not irrelevant to the debtor.

The main principle that governs the submission of claims is that only claims arising before the declaration of insolvency may be registered. Whether a claim has arisen before or after the declaration of insolvency depends on the legal basis of the claim or its cause and not on any judicial order that has established its existence. This principle does not apply to claims that arise while the company is operating on a temporary basis or claims that arise as a direct result of liquidation measures issued by the bankruptcy receiver. Therefore, future claims (ie, claims arising from an event after the declaration of insolvency) may not be registered against the assets of the bankruptcy estate. Claims that arise before the declaration of insolvency but whose amount is not established at the time of the declaration of insolvency must be quantified and proven by the creditor at the time of registration and the amount may be challenged by the bankruptcy receiver and the supervising judge during the verification of the claims. In the event a claim is rejected or is admitted for a lower sum than that requested, the

creditor may challenge the partition plan and provide evidence that it is entitled to receive the amount requested.

Conditional claims may be registered with reservations and a relevant sum is set aside pending the fulfilment or non-fulfilment of the condition. If the condition occurs, the supervising judge will, at the request of the creditor, order the admission of the claim. If the condition no longer applies, the sum previously set aside is shared among the other creditors.

A claim acquired at a discount cannot be enforced for its face value unless the creditor challenges the partial recognition of his claim and the court upholds his claim by decree.

The declaration of bankruptcy suspends the accrual of interest until the closing of the proceedings, unless the claim is secured by mortgage, pledge or privilege.

Because of such rule, a creditor cannot claim interest accrued after the opening of the insolvency proceedings.

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### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The court may change the rank (priority) of a creditor's claim only if the security on which the rank is based is null, voidable or invalid.

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### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Priority claims that rank ahead of secured claims in reorganisations and liquidation proceedings are:

- liens over moveable property, which may be either:
- general liens enforced over all the debtor's assets (such as the general lien covering the entire property of the debtor for judicial expenses, sickness, wages, taxes, etc); or
- special liens on specific assets (such as liens for customs duties on merchandise, taxes on rent, leases, etc); and
- liens on immoveable property (such as liens arising from income tax payable in relation to property, from any form of indirect taxation and other claims as indicated by specific legal provisions).

Debtors that have filed a petition for a composition with creditors (or for the validation of a restructuring agreement) may ask the court to authorise them to take out loans with priority status that will be repaid in advance of other debts. To do this, the debtor must file an expert's report with the court certifying that the loan is essential for the continuation of the business and is in the best interests of all creditors.

As mentioned above (see question 11), the debtor may also carry out acts of ordinary administration and, where authorised by the court, urgent acts of extraordinary administration during the period running from the date on which the petition for the composition with creditors is filed to the date of the decree that allows the procedure: and the law expressly provides that any debts arising as a result of such acts will have priority status.

In the extraordinary administration of large enterprises procedure, priority claims also include debts arising before the beginning of the procedure owed to small and medium enterprises for services necessary for environmental restoration, for safety reasons and for the continuity of industrial plants' activities. The same priority treatment applies to debts arising before the procedure that relate to operations concerning environmental and health protection and those provided by the Environmental Plan.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

A liquidation of a company does not automatically terminate employment contracts but they are suspended until the bankruptcy receiver or the commissioner (upon approval of the creditors' committee or surveillance committee) decides to honour their performance or terminate them.

The termination of employment contracts is a collective dismissal procedure and this will be implemented by the company.

With regard to the process and timing of a collective dismissal procedure, large-scale redundancy is governed by Law No. 223/91, which applies to companies employing more than 15 employees. This law defines a collective dismissal as being a dismissal involving at least five employees within a period of 120 days in the same province and which occurs as a consequence of the decrease or reorganisation of the business or the amount of work, or as a consequence of the total shutdown of the enterprise or business.

The employer has a duty to inform, in writing, the works council (if any) and the unions that have signed the national collective bargaining agreement applicable to the employees in Italy regarding the decision to make a collective dismissal.

A letter must be sent to the unions and must contain the following information:

- an explanation of the reason for the employer's decision;
- the number of employees likely to be dismissed;
- the positions and professional profiles of the entire workforce;
- the time frame of the redundancy; and
- any proposal or measure to reduce the possible social consequences of the redundancies.

The unions may, within seven days following receipt of the letter, request that a meeting be held to discuss the possibility of avoiding or reducing the redundancies.

If no agreement is reached, a second meeting has to take place in the following 30 days before the Labour Office. In any case, the consultation with the unions must be completed within 75 days.

At the end of the 75-day period or, if in the meantime an agreement with the unions has been reached, the employer may give notice of dismissal in writing to the employees concerned, within the usual notice periods.

Once the employees receive a dismissal letter, the notice period will begin: the length of the notice period depends on the national collective bargaining agreement applicable.

The redundancy procedure carries two types of cost for the employer:

- severance pay that includes:
- end-of-service allowance;
- other payments including accrued but untaken holiday, and other personal benefits; and
- payment in lieu of notice; and
- a potential cost of litigation arising from a claim for unfair dismissal by one or more employees (in addition to this cost an employee may also obtain reinstatement if their claim is successful).

Where a large number of employees are dismissed or where the business ceases operations the employee claims are not as a whole increased.

Claims lodged by employees for outstanding remuneration and severance pay are granted general liens on immoveable assets as are claims for damages arising from a failure to pay contributions and for damages suffered because of unlawful dismissal.

If employees' claims are not satisfied or are only partially satisfied, the employee may apply to the Guarantee Fund at the National Institute of Social Security.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

All pensions-related claims are privileged claims included within the class of liens on immoveable property. Claims arising from the employer's failure to pay contributions to pension and insurance plans managed by institutions and bodies, can be submitted by such institutions or bodies as privileged claims in the insolvency proceedings.

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**Environmental problems and liabilities**


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**36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

Neither the Insolvency Act nor the Environmental Code allocate liabilities for the control of environmental problems or remediating the damage caused. As a result, general rules apply when an environmental issue arises during insolvency proceedings. The bankruptcy receiver will operate in accordance with his powers to solve the problem under the scrutiny of the delegated judge and the creditors' committee.

Under Italian law, the party whose actions caused the pollution or contamination is obliged to implement – and finance – the remediation measures required to eliminate the contamination. Such obligations apply regardless of any intent or knowledge on the part of such a party.

Failure to take appropriate remediation measures is a criminal offence.

The owner of the contaminated site who did not cause the pollution is under no obligation to clean up the site, although he has a right to do so. If he chooses to clean up the site he assumes the same remediation obligations as the party responsible for the pollution and can claim back all damages, costs and expenses incurred in the clean-up from the responsible party.

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**Liabilities that survive insolvency proceedings**


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**37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

Following the closure of the insolvency proceedings, creditors are free to bring actions against the debtor with regard to the parts of their debts which have not been paid (although where the debtor is a natural person he or she may be freed from all remaining debts owed to unpaid creditors).

In a composition with creditors, the composition is mandatory for all creditors so where the debtor pays only a percentage of the current debts because the creditors accepted the plan they are deemed to waive their right to be reimbursed for the remaining debt. No liabilities of the bankrupt party or of the party acquiring the debtor's assets survive. This principle also applies in the case of extraordinary administration and extraordinary administration of large enterprises.

However, the creditor may still exercise its rights against co-debtors, the debtor's guarantors and with-recourse obligors.

Debt-restructuring agreements involve at least 60 per cent of the creditors and are only binding upon those creditors who have agreed to its terms since such agreements do not constitute a 'mass' composition. Therefore, any creditors that do not agree to the composition will have to be paid in full.

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**Distributions**


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**38 How and when are distributions made to creditors in liquidations and reorganisations?**

After the debtor's assets have been disposed of, the official receiver in bankruptcy, after consulting the creditors' committee, must prepare a distribution plan that is submitted to the judge for approval. Creditors have little room to challenge such a plan. The judge will approve the plan and order a distribution.

The Insolvency Act provides a mandatory order of priority for the payment of claims as follows:

- expenses of the proceedings and claims arising from the activities of the debtor during the proceedings (priority claims), which are normally paid in full when they fall due;
- secured claims over moveables and real estate; and
- unsecured claims.

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**Transactions that may be annulled**


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**39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

The provisions governing clawback or setting aside transactions in insolvency proceedings are set out in articles 64 to 70 of the Insolvency Act. Transactions and disposals that unfairly favour a single creditor at the expense of the general body of creditors (for example, by giving one a preference or other benefit at the time when the debtor is unable to pay debts) may be revoked by the court by means of a clawback action.

A clawback action is aimed at obtaining a judgment from the court that declares void and ineffective the acts performed by the insolvent debtor during the period (see question 40) immediately before the debtor was declared insolvent. Once the avoidance of the disposal of the property is established, the counterparty must return such property to the bankruptcy receiver.

Article 67(1) provides a list of transactions that can be clawed back unless the counterparty to the transaction can show it had no knowledge of the debtor's insolvent state:

- transactions in which the value of the obligations performed or assumed by the debtor exceeded one-quarter of the consideration received in exchange by the debtor (ie, transactions at an undervalue);
- payments of monetary debts past due, where the payment was not made with money or other customary payment methods;
- pledges, securities and mortgages wilfully created that were not yet past due; and
- pledges, securities and mortgages created voluntarily or by court order in respect of debts past due.

Article 67(2) provides a list of transactions that can be clawed back if the bankruptcy receiver can show that the counterparty to the transaction had knowledge of the debtor's insolvent state:

- payment of liquid and enforceable debts;
- transactions for consideration; and
- transactions giving rise to rights of pre-emption over debts, including third-party debts.

Articles 64 and 65 provide a list of additional transactions that are subject to clawback actions:

- gratuitous transfers (eg, gifts, donations); and
- payments of debts originally due on or after the date of the declaration of insolvency.

For the applicable 'suspect periods', see question 40.

Courts have taken a broad approach to determining a party's knowledge of the state of insolvency of the debtor and have ruled that if there are symptoms of insolvency such as judicial attachment, group firing of employees or press reports referring to the company's financial difficulties, the burden of proof as to the knowledge of insolvency will be shifted onto the party defending the clawback action.

Certain transactions cannot be subject to clawback actions, for example, payments for goods and services in the bankrupt party's ordinary course of business (if not otherwise unusual), remittances to a bank account not materially and permanently reducing the indebtedness to the bank, sales of real estate at fair market value, deeds and payments and securities carried out or granted to implement judicially sanctioned agreements with creditors, payments and securities carried out or granted in execution of either a composition with creditors or an agreement for the restructuring of debts approved by the court and transactions, payments and securities made after the filing of the petition for the composition with the creditors, deeds and payments carried out during the extraordinary administration of large enterprises and aimed at ensuring the business is a going concern and in the pursuit of manufacturing activity.

Where the bankruptcy receiver tries to clawback payments made under an ongoing long-term agreement or relationship (eg, an agreement for the supply of goods or services or a lease), the counterparty to the transaction may only be required to pay back an amount corresponding to the difference between the maximum amount that its aggregate claims reached in the period in which it was aware of the insolvency of the bankrupt party, and the amount of its claims on the date of the company was declared bankrupt.

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## Proceedings to annul transactions

### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The suspect periods are:

- transactions under article 67(1): one year before the opening of the insolvency proceedings;
- transactions under article 67(2): six months before the opening of the insolvency proceedings; and
- transactions under article 64: two years before the opening of the insolvency proceedings.

In general, at least four conditions must be satisfied before a transaction entered into by the insolvent company can be clawed back under the Insolvency Act:

- the company must be in insolvency proceedings;
- the transaction must have resulted in a diminution of assets available to the general body of creditors;
- the company must have been unable to pay its debts at the time of the transaction; and
- the transaction must have been entered into within the applicable suspect period.

Only the bankruptcy receiver is entitled to make a clawback action in liquidation proceedings.

Voidable transactions can also be attacked in a reorganisation procedure (extraordinary administration and extraordinary administration of large enterprises). In the case of a restructuring programme under extraordinary administration, the satisfaction of creditors is envisaged by means of a compromise under which the business is transferred to an assignee. In this case only, the extraordinary commissioner cannot make use of clawback actions nor may the assignee take the benefit of proceeds deriving therefrom.

Under extraordinary administration of large enterprises there may be an identical restructuring programme, including a compromise under which the business is transferred to an assignee, where instead the extraordinary commissioner may indeed initiate clawback actions and transfer the benefit or proceeds deriving therefrom to the assignee.

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## Directors and officers

### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Directors and officers may be held liable to the company, to the company's creditors and to third parties. Directors are liable to the company if they negligently fail to fulfil duties imposed upon them by the law or the company's by-laws. They are also liable if they fail to supervise the general conduct of the company or if, being aware of prejudicial acts, they did not do what they could to prevent such acts from occurring. However, they cannot be made to pay obligations owed by their corporations.

When a company is insolvent its directors have a duty to avoid making preferential payments, not to continue trading in a way that would be detrimental to the financial position of the company and, if the statutory minimum share capital is lost, not to enter into new transactions. The directors will be jointly and severally liable for any breach of these duties.

If these duties are breached, the company's shareholders in a general meeting or, for listed companies, shareholders representing at least 5 per cent of the share capital, may resolve to bring a civil action for damages.

Directors are also liable to the company's creditors when the company's assets are insufficient to satisfy their claims because the directors have failed to preserve the company's assets. Such actions do not prevent single shareholders or third parties from bringing claims for damages if they are directly damaged by the directors' conduct.

Directors and de facto officers (as well as statutory auditors) may be charged with criminal liability for 'fraudulent bankruptcy' where a company has gone into judicial liquidation if they:

- have disposed and transferred all or part of the company's assets with intent to defraud creditors of the company;
- have destroyed or falsified all or part of the corporate books or other accounting records; or
- before or during the judicial liquidation proceedings they have made payments with intent to prefer one or more creditors.

The criminal sanction for 'fraudulent bankruptcy' is imprisonment for between three and 10 years and disqualification from acting as a director for 10 years.

Directors may be liable for 'simple bankruptcy' if they:

- have carried out high-risk transactions with the intent of delaying the commencement of bankruptcy proceedings;
- have increased the company's liabilities by failing to file a petition for the commencement of the insolvency proceedings when the company was insolvent or over-indebted; or
- during the three years preceding the declaration of insolvency, did not keep the corporate books and the other accounting records prescribed by the law.

The criminal sanction for 'simple bankruptcy' is imprisonment for between six months and two years and disqualification from acting as a director for up to two years.

There are some exemptions for bankruptcy offences including in respect of payments and transactions carried out to implement a composition with creditors, or an agreement on debt restructuring, or a plan aimed at the reorganisation of the company's debts and ensuring recovery from the financial distress.

Criminal liability may occur if directors and general managers, by hiding the company's crisis and insolvency, continue to obtain loans from credit institutions. Article 218 of the Insolvency Act provides for between six months' and three years' imprisonment and disqualification from acting as a director for up to three years. An increased penalty is provided where the company acts as a financial intermediary on the market.

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## Groups of companies

### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

The only case where a corporation can be held responsible for the liabilities of another company is when, while exercising an activity of management and coordination, it has acted in a manner contrary to the principles of sound company management and thereby caused damage to the other company's assets. Despite the general principle of 'perfect patrimonial autonomy' based on which a parent or affiliated corporation will not be liable for the subsidiaries or affiliates' debts, the bankruptcy receiver is entitled to exercise the same rights as the bankrupt company's creditors and has the right to submit a claim against the parent company on behalf of the bankrupt company's creditors. The same liability may be extended to other entities of the group that were involved in the unlawful act or benefited from it.

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## Insider claims

### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

For Srl companies (limited liability companies) the reimbursement of shareholder loans must be postponed with respect to all other debts of the company and if any sums were reimbursed in the year before the company was declared bankrupt, the amount reimbursed must be returned to the company.

This applies to any type of financing granted to the company by its shareholders 'in circumstances where – even considering the business activity carried out by the company – there is an excessive unbalance between company's indebtedness and its net assets or where an equity contribution would have been more reasonable'.

According to academics and case law, the provision includes shareholder funds injected in situations where the company appears undercapitalised at the time of the financing and thus has the 'substance' of

an equity contribution and operates regardless of the relevant shareholder's knowledge of the company's financial situation

The provision also applies to intercompany loans, and in particular to funds granted to the company (either joint-stock company – SpA – or Srl) by its parent company. According to some academics, the provision also applies to loans made by a sole shareholder, even if the company is a joint-stock company (SpA) and not an Srl, since there would be no reason for treating the same situation in a different way according to the type of company.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Insolvency proceedings are aimed at satisfying the claims of a company's creditors. Their effect is that the creditors are prohibited, following the declaration of bankruptcy, from filing executive or interim claims over the assets of the insolvent debtor outside the bankruptcy procedure. In line with this principle, all individual enforcement proceedings are suspended in the event of insolvency, save for enforcement proceedings relating to certain mortgage loans that are subject to specific Italian registration.

There are particular rules for debts secured by liens or pledges, which may even be recovered by the relevant creditor during the insolvency proceedings, provided they are included in the insolvency estate with priority status, through the direct sale of the asset. To obtain authorisation for the asset to be sold the creditor must file a petition with the supervising judge, who, having heard the bankruptcy receiver and creditors' committee, will issue an order detailing the timing and the procedure for the sale.

Outside insolvency proceedings, the assets of a business can be seized only within judicial proceedings.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Dissolution of a company may be voluntary, in which case the courts are not involved and the rules set out by the Civil Code apply. Dissolution occurs upon verification of conditions set out in the law, in the company's by-laws or upon the passing of a resolution at a shareholders' extraordinary meeting (see question 9).

The main difference between voluntary and mandatory dissolution is that, by virtue of the principle of non-discrimination among creditors, the Insolvency Act grants special protection to creditors, specifically the prohibition to file individual claims, the clawback action, etc.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Both voluntary liquidation procedures and insolvency procedures are concluded when the proceeds from the disposal of the assets are distributed to creditors. In a voluntary liquidation, the liquidators must draft and deposit financial statements relating to the liquidation process. The company will then be removed from the Register of Companies. In an insolvency procedure, the court issues a formal order that declares the proceedings closed. The main effect of the order is that creditors whose claims have not been fully satisfied may initiate or continue individual enforcement proceedings over the debtor's residual assets and the debtor may restart its business.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

For procedures opened in a member state of the European Union the opening of insolvency proceedings in that member state shall be recognised in all other member states. Recognition of the procedure shall not preclude the opening of insolvency proceedings in another member state concerning assets of the debtor situated in that territory (secondary proceedings).

A member state may refuse to recognise or enforce a judgment handed down in insolvency proceedings of another member state where the effects of such recognition or enforcement would be manifestly contrary to that state's public policy, especially when its effect is to restrict fundamental rights and freedoms, or on the grounds of public policy where the principles of due process have been breached (ie, breach of defence rights and the principle of *audi alteram partem* – impartiality of the court).

Where the insolvency proceedings are not subject to EU legislation there are two possible alternatives:

- the effects of the insolvency declared abroad may be extended to Italy where the insolvency officeholder or the creditors apply for recognition of the foreign declaratory judgment and the order detailing the estate; or
- the bankruptcy receiver or the creditors may request an independent declaration of insolvency in Italy, with the risk that there may be conflicts and interferences between the two proceedings. Indeed, the insolvency officeholder and the creditors involved in the foreign insolvency proceedings could lodge any claims admitted abroad in the Italian proceedings if they first obtain interlocutory rulings recognising such orders. However, the foreign creditors, like the Italian creditors, could also lodge independent claims in the Italian insolvency proceedings. Likewise, the Italian bankruptcy receiver could lodge claims under the same terms against the estate in the foreign insolvency proceedings.

Foreign insolvency judgments and orders may be recognised by Italian courts with immediate effect if certain conditions are met. The competent court of appeal will declare the foreign judgment enforceable in Italy if:

- the foreign court was competent to issue the judgment according to Italian law on jurisdiction;
- the defendant received adequate notice and was afforded sufficient time to appear in accordance with the law of the foreign tribunal;
- the parties in the foreign action appeared or the absence of either party was properly taken into account in accordance with the law of the foreign tribunal;
- the foreign judgment was final (ie, not subject to appeal);
- the foreign judgment is not in conflict with a final judgment handed down by an Italian court;
- the parties are not litigating the same matter before an Italian court in proceedings started before the beginning of the foreign proceedings; and
- the foreign judgment is not contrary to Italian rules of public policy and public order.

There are still some uncertainties regarding the practical implications and consequences for insolvent debtor's assets in Italy, but the unresolved issues seem to be similar to those common in other jurisdictions.

Foreign creditors are subject to the same regime applicable to national creditors.

Legislation based on the UNCITRAL Model Law on Cross-Border Insolvency has not yet been adopted.

**COMI****48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

The Insolvency Act says nothing about how to determine the COMI of a debtor company or group of companies. Thus, references should be made to the European Court of Justice (ECJ) case law. The EC Regulation on Insolvency Proceedings (the Regulation) does not contain a definition of 'COMI' but the recitals to it state that the COMI should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore ascertainable by third parties. The Regulation applies the concept of COMI to each individual debtor and not to a group of companies – which can all have individual COMIs. See further the chapter on the European Union.

The two most important cases in which the Italian courts considered the concept of COMI recently were *Re Eurofood IFSC Ltd* (C-341/04) of 2 May 2006 and *Interedil Srl (in liquidation) v Fallimento Interedil Srl and another (Interedil)* (Case C-396/09) of 20 October 2011.

In *Eurofood*, the Irish Supreme Court referred questions to the European Court of Justice in relation to the insolvency of the Parmalat group of companies in Italy. In particular the question was whether a subsidiary of Parmalat (Eurofood), registered in Ireland, should be liquidated in Ireland or in Italy. Eurofood's principal business was the provision of financing facilities for Parmalat. Shortly after Parmalat went into administration, a creditor applied to the Irish High Court for it to be compulsorily wound up in Ireland. The Irish court considered that Eurofood's COMI was in Ireland and appointed a provisional liquidator. Two weeks later, the Italian court decided that it had jurisdiction because Eurofood's COMI was in Italy, and Eurofood was admitted to the Italian administration procedure.

The ECJ held that main insolvency proceedings opened by a court of a member state had to be recognised by the courts of the other member states, without the latter being able to review the jurisdiction of the former court. Further, where a subsidiary company and its parent were registered in different member states and the subsidiary carried on its business in the member state where it was registered, the article 3(1) presumption in the Regulation that a debtor's COMI was in that member state was not rebutted by the parent company's having control over the subsidiary's policy.

In the case of *Interedil* the ECJ confirmed that COMI must be interpreted in a uniform way by EU member states and by reference to EU law and not national laws. Here the company had been incorporated under Italian law, transferred its registered office from Italy to the United Kingdom. After the company had ceased all activity and had been removed from the United Kingdom register, a creditor filed winding up proceedings with a court in Italy. The company opposed those proceedings on the ground that based on its COMI in the United Kingdom, the United Kingdom had jurisdiction to open insolvency proceedings. On the creditor's application for a preliminary ruling as

to the jurisdiction of the Italian courts to open insolvency proceedings, the Supreme Court of Cassation held that the presumption in article 3(1) that the COMI corresponded to the place of the debtor's registered office in the UK was rebutted by the presence of immovable property in Italy owned by the company and in respect of which it had concluded a lease agreement. The Italian court held that decision was different to the case law of the ECJ, but that it was nevertheless bound by it under the Italian law. The ECJ held that European Union law precluded a national court from being bound by a national procedural rule under which the court was bound by the rulings of a higher court, where it was apparent that the rulings of the higher court were at variance with European Union law. The ECJ further held that the term 'COMI' was a term peculiar to the Regulation and has an autonomous meaning.

In summary, where a company's registered office and place of central administration are in the same jurisdiction, the registered office presumption set out in the recitals to the Regulation cannot be rebutted. Where a company's central administration is not in the same place as its registered office, the presence of assets belonging to the debtor and the existence of contracts for financial exploitation of those assets in an EU member state, other than that in which the registered office is situated, are not sufficient factors to rebut the registered office presumption, unless a comprehensive assessment of all the relevant factors makes it possible to establish, in a manner that is ascertainable by third parties, that the company's central administration is located in that other EU member state.

Factors that have been held to be relevant to determine a debtor's COMI (in addition to the rebuttable registered office presumption) are: location of internal accounting functions and treasury management, governing law of main contracts and location of business relations with clients, location of lenders and location of restructuring negotiations with creditors, location of human resources functions and employees as well as location of purchasing and contract pricing and strategic business control, location of IT systems, domicile of directors, location of board meetings and general supervision.

**Cross-border cooperation****49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

In Italy, there is a good level of coordination and cooperation between the various courts involved in Italian bankruptcy proceedings taking place in different cities.

As for collaboration with other jurisdictions, there is a Franco-Italian Protocol that aims to regulate the exchange of information and collaboration between bankruptcy receivers in Italy and France.



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The case law reveals a generalised application of the principle of recognition of judgments declaring insolvency. In this regard, the following rulings may be of interest:

- the Court of Appeal of Turin reiterated the principle that ‘the main insolvency proceedings opened in one member state must be recognised by the courts of the other member states, which does not verify the jurisdiction of the court of the member state in which the proceedings were opened’;
- the Court of Milan stated that insolvency proceedings opened against an investment company in the member state in which it has its headquarters is automatically effective in Italy (in that case: an administration procedure in the United Kingdom);
- the Court of Naples held that recognition of a foreign judgment that opened insolvency proceedings does not imply that such decision has the same effectiveness in Italy as an Italian insolvency ruling, since it is necessary to take into account the effects produced in the country of origin; and
- the Court of Milan, applying German rules, recognised that the payment of a certain sum of money by the debtor in the three months preceding the application for the opening of insolvency proceedings, following the creditor’s warning that it would submit the application in the event of a default, could be clawed back if the debtor was not in a position to fulfil its obligations.

With regard to the jurisdiction for declaring a company insolvent, the following decisions are significant:

- the Court of Rome declared the insolvency of Cirio Del Monte NV, whose registered office was in Holland and which was a wholly owned subsidiary of an Italian parent that had already been declared insolvent, on the grounds that its operational and executive centre was situated in Italy, where all the Italian members of the board of directors were resident.
- the Court of Parma, within the context of the insolvency of the Parmalat group, held that it had jurisdiction to declare the insolvency of Parmalat Neth BV, a company of the group whose registered office was in the Netherlands, on the grounds that the executive activities and operational centre of the company were located in Collecchio, at the headquarters of the parent. It concluded that the Dutch company was merely a vehicle for the financial policy of Parmalat SpA, which was created for the sole purpose of facilitating money flows.

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#### Cross-border insolvency protocols and joint court hearings

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

Italian courts have not entered into any cross-border protocols to coordinate proceedings with courts in other countries.

# Japan

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## Legislation

- 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?**

### Liquidation

The applicable legislation is:

- for bankruptcy procedures, the Bankruptcy Law (Law No. 75 of 2004); and
- for special liquidation procedures, articles 510 to 574 of the Companies Act (Law No. 86 of 2005).

### Reorganisation

The applicable legislation is:

- for civil rehabilitation procedures, the Civil Rehabilitation Law (Law No. 225 of 1999); and
- for corporate reorganisation procedures, the Corporate Reorganisation Law (Law No. 154 of 2002).

A debtor is insolvent (more accurately a bankruptcy event under the Bankruptcy Law has occurred with respect to the debtor) if it is unable to pay its debts (by reference to its financial position, following a calculation of whether the debtor is generally able to pay all debts already due on a certain date) or the debts it owes exceed its assets (by reference to its financial position, following a calculation of whether the aggregate amount of the debtor's debts exceeds the aggregate amount of its assets – this is only applicable to corporations).

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## Courts

- 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?**

In general, insolvency procedures are heard before the District Court. If there is a conflict of jurisdiction between two or more courts, the procedure will be heard at the court in which the petition was first filed.

### Bankruptcy procedure and civil rehabilitation procedure

For a business entity debtor, the district court whose jurisdiction covers the debtor's main business office in Japan has exclusive jurisdiction. If there is no such place, the district court that has jurisdiction is that in which the assets are located.

The following special rules apply to bankruptcy and civil rehabilitation procedures:

- a petition of bankruptcy or civil rehabilitation may be filed at any district court dealing with the ongoing bankruptcy or civil rehabilitation procedure of a parent or subsidiary company, a consolidated affiliate, or a representative of the debtor company;
- a petition of bankruptcy or civil rehabilitation may be filed at the district court that is currently dealing with any ongoing bankruptcy procedure or civil rehabilitation procedure relating to a joint debtor, a guarantor or married couple, and vice versa, if the procedure relating to the other party is ongoing;
- if the number of creditors is 500 or more, a petition of bankruptcy or civil rehabilitation may be filed at the main district court in a region, provided that another district court in the region has jurisdiction (eg, the Tokyo District Court has jurisdiction, if a petition

can be filed to the Yokohama District Court, which is within the jurisdiction of the Tokyo High Court); and

- if the number of creditors is 1,000 or more, a petition of bankruptcy or civil rehabilitation may be filed at the Tokyo or Osaka District Court.

### Corporate reorganisation procedure

A petition to commence a corporate reorganisation procedure may be filed at:

- any district court in which the debtor has its main business office in Japan;
- any district court in which the debtor has its head office;
- any district court in which the ongoing corporate reorganisation procedure of a parent or a subsidiary company or a consolidated affiliate is being dealt with; or
- the Tokyo or Osaka District Court.

### Special liquidation procedure

Under this procedure, the district court that will have exclusive jurisdiction is that in which head office of the company is located. A petition for special liquidation of the debtor may be made at any district court dealing with the ongoing special liquidation, bankruptcy, civil rehabilitation or corporate reorganisation procedure of a parent company.

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## Excluded entities and excluded assets

- 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?**

The special liquidation procedure and corporate reorganisation procedure are only available to joint-stock companies. The bankruptcy procedure and civil rehabilitation procedure are available to both individuals and corporations. Permanent entities such as national or local governments are excluded from insolvency procedures.

Financial institutions such as banks, credit banks or credit cooperatives are not exempted from the insolvency procedures. There are, however, special procedures under the Deposit Insurance Law that provide a system for distressed financial institutions to be rebuilt and for the control of the institution to be transferred to a different entity under the supervision of a financial reorganisation receiver.

In addition, the Act on Special Treatment of Corporate Reorganisation Proceedings and Other Insolvency Proceedings of Financial Institutions, which refers to, supplements and restates the Corporate Reorganisation Law, the Civil Rehabilitation Law and the Bankruptcy Law, is applicable to banks and insurance companies which are joint-stock companies and financial institutions in other legal forms such as credit banks, credit cooperatives, labour credit associations and insurance companies incorporated as mutual companies.

All of the assets a debtor owns as of the commencement of the relevant insolvency proceeding are subject to such insolvency proceeding except that:

- in a bankruptcy proceeding and if the debtor is an individual, cash up to ¥440,000 and moveable assets that a creditor is prohibited from attaching are excluded; and

- (except in a corporate reorganisation proceeding) claims secured by a special preferential right, a pledge, a mortgage, a lien under the Commercial Code or any other security interests, such as a security by way of transfer existing over the assets of a debtor, may be exercised outside the bankruptcy procedures.

If a debtor holds assets that are owned by a third party (eg, a broker holds shares for its customer) such third party has the right to request the return of such assets.

### Public enterprises

#### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There is no special procedure for the insolvency of a government-owned enterprise. A government-owned enterprise is subject to the same insolvency and reorganisation procedures as standard companies; namely, bankruptcy, special liquidation, civil rehabilitation and corporate reorganisation.

### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Article 102 of the Deposit Insurance Law allows the government to (i) inject capital into a bank; (ii) guarantee deposits not covered by deposit insurance held by a bank; or (iii) nationalise a bank, or any combination of these, if it is determined that the failure of the bank severely jeopardises the maintenance of the credit order in Japan or the region in which the bank operates.

### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

The principal types of security that can be taken on immoveable (real) property are:

- mortgage – a mortgage, as set out in the Civil Code, gives a creditor the right, evidenced by an agreement, to enforce the payment of a debt against a debtor by asking the court to conduct a public auction of the real property that secures the debt and taking the proceeds of that auction. As a result of the ability to force the sale of the real property, the creditor has priority over other creditors. The creditor's priority is established by the registration of the mortgage at the land registry;
- pledge – a pledge may be given over real property; generally, however, a mortgage as described above is used. See question 6 for pledges on moveable property;
- preferential right – as set out in the Civil Code, preferential rights are a series of security devices that automatically secure certain types of claims (eg, unpaid wages). There are two categories of preferential rights: general preferential rights securing all relevant assets and special preferential rights securing particular goods or real property; and
- security by way of transfer – a type of security approved by Japanese courts but not specifically set out in the Civil Code. A security by way of transfer involves the transfer of the legal ownership of the subject matter (including real property) of the security from the debtor to the creditor at the time that the security is created, subject to the debtor's right to redeem the subject matter of the security if and when the relevant debt is paid in full. A security by way of transfer allows the debtor to continue to use the secured asset until the creditor enforces the security.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The principal types of security that can be taken on moveable (personal) property are:

- pledge – a pledge, as set out in the Civil Code, can be created over both tangible and intangible assets (such as claims and patents,

etc). The pledgee controls the pledged assets in the case of tangible assets by physical possession; or in the case of intangible assets by registration, notice to or consent from the third-party debtor (or such other means as appropriate for the type of assets pledged). The pledgee can satisfy its claim by the disposal of the pledged assets (including through a private auction) if the pledgor does not pay any outstanding debts that are secured by the pledge;

- lien – as set out in the Civil Code and the Commercial Code, the right of a creditor to retain the property of the debtor to which a claim relates until the debt is paid;
- reservation of ownership – not set out in the Civil Code, but a type of security approved by Japanese courts. This allows a seller of goods to retain ownership of these goods until it receives payment in full. Once the buyer pays the purchase price owed for the goods, the ownership of the goods is transferred to the buyer; and
- preferential right or security by way of transfer (see question 6).

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

An unsecured creditor may bring compulsory execution procedures at the appropriate district court, by filing a debt claim for any of the following: a fixed judgment; a judgment with a declaration of provisional execution; a payment order (summary order by the court clerk) with a declaration of provisional execution; or a notarial document with an agreement of execution, together with documentation of execution. Under the compulsory execution procedures, the district court will arrange for the property that is the subject of the debt claim to be auctioned.

The quickest procedure available to an unsecured creditor is to obtain a notarial document with an agreement of execution from a notary public. This notarisation can be prepared at a notary public office and a notary fee depends on the amount of consideration for the relevant agreement. A payment order may also be obtained from the court clerk in a relatively short period if the debtor does not raise any objections. However, it may take longer (eg, may take several months) to obtain a fixed judgment or a judgment with a declaration of provisional execution because an unsecured creditor must follow ordinary litigation procedures.

To prevent a debtor from disposing of its assets prior to completion of the litigation procedures before obtaining a fixed judgment or a judgment with a declaration of provisional execution to the debtor, an unsecured creditor may file a provisional attachment, under which an unsecured creditor may have any disposal of the debtor's property declared legally invalid.

Once the competent court has declared an insolvency procedures have commenced with respect to a debtor, an unsecured creditor of the debtor is no longer able to carry out compulsory execution (subject to certain exemptions such as set-off below). No special procedures apply to foreign creditors.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

##### Liquidation procedure

Under the Companies Act, a company can be dissolved by a special resolution at a shareholders' meeting.

After dissolution, the company will automatically go into liquidation. The company is no longer able to conduct business but continues to exist until the liquidation is completed.

The liquidation procedure is managed by a liquidator who is supervised by the court. Unless another person is appointed by a shareholders' resolution or by operation of the articles of incorporation, the company's directors assume the role of liquidators.

During the liquidation, all of the assets of the company are sold to raise funds for distribution to creditors and shareholders. Creditors are repaid in full. If the company's debts exceed its assets, the company must shift into the special liquidation procedure (see question 10). After the completion of repayment to the company's creditors,

shareholders will receive distribution of remaining assets pro rata to their respective shareholding.

### Bankruptcy procedure

In the case of individual bankruptcies, the individual, and in the case of corporate bankruptcies, a director of such company, may file a bankruptcy petition with the court. A fee of ¥1,000 and a deposit, determined by the court, must be paid to cover the costs of the bankruptcy procedures.

The bankruptcy procedures may be commenced if:

- a debtor is unable to pay its debts (by reference to its financial position, following a calculation of whether the debtor is generally able to pay all debts already due on a certain date); or
- debts a debtor owes exceeds its assets (by reference to its financial position, following a calculation of whether the aggregate amount of the debtor's debts exceeds the aggregate amount of its assets – this is only applicable to corporations).

When a bankruptcy petition is filed, the court may, prior to the commencement of the procedure, order the discontinuance of any ongoing litigation procedures or administrative procedures relating to the assets of the debtor. Discontinuance of compulsory executions, executions of a provisional attachment or a provisional disposal or auctions based on a lien (other than liens under the Commercial Code) against the assets of the debtor, which are based on claims that may not have a priority under the bankruptcy procedure, may be ordered either with respect to individual assets or to all assets, unless such discontinuance causes unjustifiable damage to creditors.

The court may also order a discontinuance of any ongoing execution of corporate security rights against the debtor's assets that are based on claims that may not have a priority under the bankruptcy procedure (ie, enforcement of such security rights would be prohibited); or the debtor's liability limitation procedure with respect to the Shipowners Law and the Oil Pollution Compensation Law, for which the court has not ordered the commencement of the debtor's liability limitation procedure.

The court may also grant orders imposing provisional attachments, provisional disposals or any other necessary measures to preserve the debtor's business and assets. In addition, exercising secured claims may be prohibited by the court prior to the commencement of the procedure.

If the debtor falls within the grounds of one of the two conditions above under which a bankruptcy procedure may be commenced, the court will order the commencement of the procedure and simultaneously appoint a trustee-in-bankruptcy.

If the remaining assets of the debtor are not sufficient to cover the cost of the procedure, the court will conclude the procedure and will not appoint a trustee (then the debtor company will shift to a liquidation procedure). A corporation can be appointed as a trustee-in-bankruptcy but one or more lawyers are usually appointed as the trustees in bankruptcy.

On commencement of the bankruptcy procedure, the assets of the debtor form the bankrupt estate. The trustee administers the bankrupt estate in place of the debtor.

Once the court orders the commencement of the bankruptcy procedure, claims against the bankrupt debtor that existed prior to the commencement of the bankruptcy procedure may only be enforced through the bankruptcy procedure. Ongoing procedures such as compulsory execution or executions of provisional attachments, provisional disposals or corporate security rights against the bankrupt estate will become invalid.

Claims secured by a special preferential right, a pledge, a mortgage, a lien under the Commercial Code or any other security interests, such as a security by way of transfer, existing over the assets of a debtor, may be exercised outside the bankruptcy procedures. Further, a creditor may exercise the right of set-off if a creditor owes a debt to a debtor at the time of the commencement of the bankruptcy. There is a possibility that the court may approve the extinction of certain security rights on a debtor's assets with the exchange by the trustee of the relevant amount of cash equivalent to the proceeds of a sale of the assets less an amount set aside for the bankrupt estate, if selling such assets and dissolving certain security rights match the general interests of creditors and do not unjustifiably harm the interest of the creditor who has the security rights on such assets.

### Special liquidation procedure

Again, the special liquidation procedure is only available to joint-stock companies. The special liquidation procedure may be commenced if a joint-stock company is already in liquidation and:

- it is found that there is a significant impediment to the liquidation procedure (eg, if the assets and debts of the company are very complex); or
- it is suspected that the company's debts exceed its assets.

A liquidator may file a petition for special liquidation at the court. Usually, a director of the company will become the liquidator after dissolution of the company. A liquidator must be an individual. A fee (¥20,000) and a deposit, decided by the court, are payable to cover the costs of the special liquidation procedure.

If a petition is filed, the court may grant an injunction to preserve the assets of the company, to prohibit any changes to the registry of shareholders or to preserve the assets of promoters, directors, liquidators or auditors, prior to the commencement of the special liquidation procedure.

Once the court has ordered commencement of a special liquidation procedure, the debts of the company must be paid to creditors in proportion to the amount of their claims. Petitions of bankruptcy, compulsory execution or executions of provisional attachments or provisional disposals are prohibited during the special liquidation procedure and any ongoing procedures of such nature will cease automatically upon commencement of the special liquidation procedure.

However, claims secured by a special preferential right, a pledge, a mortgage, a lien under the Commercial Code or any other security interests, such as a security by way of transfer, existing over assets of a debtor, and a general preferential right such as a lien under the Civil Code or a corporate security right can be exercised outside the special liquidation procedure. A creditor may also exercise a right of set-off if a creditor owes a debt to a debtor at the time of the commencement of the special liquidation.

Upon commencement of the special liquidation procedure, a liquidator may still continue as a liquidator under the supervision of the court. However, when the special liquidation procedure begins, a lawyer, in addition to or instead of the original liquidator, is usually appointed as a liquidator by the court.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

##### Bankruptcy procedure

A creditor of a company may file a bankruptcy petition with the court. A fee (¥20,000) and a deposit, decided by the court, must be paid to cover the costs of the procedure. In addition, a creditor must prove prima facie to the court that it has a valid claim against a debtor and that grounds for bankruptcy exist. The grounds for and the effects of involuntary bankruptcy are the same as for the voluntary bankruptcy procedure, as are other aspects of the subsequent process.

##### Special liquidation procedure

A creditor, liquidator, statutory auditor or shareholder of the company that is already undergoing liquidation may file a petition to commence a special liquidation procedure with the court. A fee (¥20,000) and a deposit, determined by the court, must be paid to cover the costs of the procedure. The grounds for and the effects of involuntary special liquidation are the same as for voluntary special liquidation, as are other aspects of involuntary special liquidation.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

##### Civil rehabilitation procedure

The purpose of the civil rehabilitation procedure is to enable a debtor in financial difficulties to pay its debts and continue its business by obtaining the court-sanctioned consent of creditors who are owed a substantial portion of the debts.

A debtor may file a petition for civil rehabilitation with the court. A fee (¥10,000) and a deposit, determined by the court, must be paid to

cover the costs of the civil rehabilitation procedure. In addition, a debtor must prove prima facie to the court that the grounds for civil rehabilitation exist.

The civil rehabilitation procedure may be commenced if:

- there is a significant likelihood that a bankruptcy event will occur (see question 9 for a list of bankruptcy events); or
- the debtor is unable to pay its debts already due on a certain date without substantially impeding its ability to carry on its business.

When the petition is filed, the court will usually order a preservation measure under which the payment of debts and granting of security to creditors (other than payment of taxes, salaries, utility bills, office rents, lease fees for office equipment, debts under a certain threshold and other items specified by the court) are prohibited.

The court will also appoint a supervisor. Certain types of corporate actions specified by the court (which include the transfer and disposal of assets, the receipt of assets, the borrowing of money and the giving of guarantees and the assumption of liabilities) will be restricted by the court and require the supervisor's approval.

In addition, when a civil rehabilitation petition is filed, the court may, prior to the commencement of the procedure, order a discontinuance of any ongoing bankruptcy, special liquidation, litigation or administrative procedures relating to the assets of the debtor. Discontinuation of compulsory executions, executions of a provisional attachment or a provisional disposal or auctions based on a lien (other than liens under the Commercial Code) against the assets of the debtor may be ordered either with respect to individual assets or to all assets, unless such discontinuation causes unjustifiable damage to creditors. The court may also grant orders imposing provisional attachments, provisional disposals or any other necessary measures to preserve the debtor's business and assets. Furthermore, exercising secured claims may be prohibited by the court prior to the commencement of the procedure.

If the debtor falls within the grounds of one of the two conditions above under which a civil rehabilitation may be commenced, the court will order the commencement of the procedure. Before making an order for the commencement of the civil rehabilitation procedure, the court must hear opinions from a labour representative (such as a labour union), except where it is obvious to the court that the petition should be dismissed or there are prima facie grounds to commence the civil rehabilitation proceedings. As a general rule, under the civil rehabilitation procedure the debtor will remain in charge of its business. As explained above, a supervisor is appointed in most cases to approve certain activities as specified by the court. If the court deems it necessary, it can appoint an administrator (rather than a supervisor) who will operate the debtor's business and administer all of the debtor's assets which means the debtor company loses day-to-day control of the business. A corporation can be appointed as a supervisor and administrator.

Once the court orders the commencement of the civil rehabilitation procedure, rehabilitation claims (claims against the debtor's assets that exist prior to the commencement of the civil rehabilitation procedure and other specific claims against the debtor set out under the Civil Rehabilitation Law, such as a claim for interest, that arise after the commencement of the procedure) may not be paid out, received or extinguished (excluding by waiver of the claim by the creditor) other than in accordance with the rehabilitation plan, unless otherwise specified in the Civil Rehabilitation Law, such as paying claims of small companies whose main customer is the debtor (only if the business of such a small company is likely to suffer significant damage if debts owed to it are not repaid immediately) or claims of small amounts with the permission of the court. Petitions for bankruptcy, civil rehabilitation, special liquidation or compulsory executions, executions of provisional attachment or provisional disposal or auctions based on a lien (other than liens under the Commercial Code) against the assets of the debtor are prohibited. Ongoing procedures of the type previously mentioned are discontinued or lose effect automatically. Any litigation procedure or administrative procedure relating to the assets of the debtor will be suspended at the commencement of the civil rehabilitation procedure.

Claims secured by a special preferential right, a pledge, a mortgage, a lien under the Commercial Code or any other security interests, such as a security by way of transfer, existing over the properties of the debtor, shall be exercised outside the civil rehabilitation procedure unless the court prohibits the exercise of such security rights pursuant to the Civil Rehabilitation Law (this is different from the corporate

reorganisation procedure below under which enforcement of security will be restricted). A creditor may execute a right of set-off until the due date of the claim filing period if a creditor owes a debt to a debtor at the time the procedure commences.

There is a possibility that the court may approve the release of certain security rights on a debtor's assets with the exchange by the debtor of the relevant amount of cash equivalent to the value of the assets subject to such security rights, if the assets are essential for a debtor to continue its business.

### Corporate reorganisation procedure

The purpose of the corporate reorganisation procedure is to enable a company in financial difficulty to reconstruct its business by involving all relevant parties in a reconstruction process sanctioned by the court. The corporate reorganisation procedure is available for Japanese joint-stock companies and foreign joint-stock companies that have business premises in Japan and is designed to be used by a large corporation whose bankruptcy would have a significant adverse effect on society.

A joint-stock company may file a corporate reorganisation petition with the court. A fee (¥20,000) and a deposit, determined by the court, must be paid to cover the costs of the corporate reorganisation procedure. In addition, a debtor company must prove prima facie to the court that grounds exist for corporate reorganisation. The grounds for corporate reorganisation are similar to those for civil rehabilitation. When the petition is filed, the court will usually issue a preservation and administration order and appoint a lawyer as preservation administrator and order him or her to operate the business of the debtor company and manage the debtor company's assets until the commencement of the corporate reorganisation procedure.

Under the preservation and administration order, the preservation administrator will be required to seek court approval for certain activities specified by the court, such as payments of debts to creditors (except for items specified by the court), the disposal of assets, borrowing of money, any waiver of important rights and any alteration of collateral granted on the debtor company's assets.

The court may also, before the commencement of the procedure, order the discontinuance of any ongoing bankruptcy, civil rehabilitation or special liquidation procedures, the exercise of corporate security rights and litigation or administrative procedures relating to the assets of the debtor. Discontinuation of compulsory executions or executions of provisional attachments, provisional disposals, enforcement of security rights or auctions based on liens against the assets of the debtor may be ordered with respect either to individual assets or to all assets, unless such discontinuation causes unjustifiable damage to creditors. Further, the court may order a provisional disposal or any other necessary measures to preserve the debtor's business and assets.

If the company falls within the grounds under which a corporate reorganisation procedure may be commenced, the court will order the commencement of the corporate reorganisation procedure. Before making an order for the commencement of the corporate reorganisation procedure, the court must hear opinions from a labour representative (such as a labour union), except where it is obvious to the court that the petition should be dismissed or there are prima facie grounds to commence the corporate reorganisation procedure. An administrator is always appointed simultaneously upon the commencement of a corporate reorganisation procedure and immediately assumes responsibility for the operation of the business and management of the debtor company's assets under the corporate reorganisation procedure.

The court has recently been trying to introduce the practice of a debtor-in-possession (DIP) type corporate reorganisation under which a member of the existing management of the debtor company will be appointed as an administrator, if:

- the management were not involved in illegal or unjustifiable activities;
- major creditors are not opposed to the appointment of a member of management as the administrator;
- a sponsor (if any) has agreed to the appointment of a member of management as the administrator; and
- implementation of the proceedings would not be impaired by appointing a member of management as the administrator.

Under this type of corporate reorganisation, a preservation administrator will not be appointed and a member of the existing management

continues to operate the business during the period from filing to the commencement of the proceedings. Instead, the court will issue a supervision and investigation order and appoint a lawyer as a supervisor and investigator to monitor and investigate the business operated by the management. Under the supervision and investigation order, certain types of activities that fall outside the scope of the ordinary course of business as specified by the court (eg, disposal of assets, acquisition of assets, making loans, filing a lawsuit with the court, settlement of claims and arbitration, waiver of rights and alteration of security granted over the debtor company's assets) will be restricted by the court and require the supervisor and investigator's approval. The court will also issue a preservation order under which the payment of claims that existed before the petition was filed and the granting of security with respect to such claims become subject to court approval with the same exceptions (eg, payment of salaries and payment of liabilities below a certain de minimis threshold and other items specified by the court). In addition, when the petition is filed, the court will sometimes issue a cessation order freezing the enforcement of the security interests in order to cover the period until the commencement of the proceedings, at which time the enforcement of the security interests will be prohibited by operation of law.

Once the court orders the commencement of the corporate reorganisation procedure, reorganisation claims (claims against the debtor's assets existing prior to the commencement of the corporate reorganisation procedure and other specific claims against the debtor set out under the Civil Rehabilitation Law, such as a claim for interest, arising after the commencement of the procedure) may not be paid out, received or extinguished (excluding by waiver of the claim by the creditor) without following the reorganisation plan unless otherwise specified in the Corporate Reorganisation Law, such as paying claims of small companies whose main customer is the debtor (only if the business of such small company is likely to suffer significant damage if debts owed to it are not repaid immediately) or claims of small amounts with the permission of the court. Petitions for bankruptcy, civil rehabilitation, corporate reorganisation, special liquidation, compulsory execution, executions of provisional attachment or provisional disposal, execution of security rights, auctions based on lien or corporate security rights are prohibited and ongoing procedures of this type shall be discontinued or lose effect automatically.

Any litigation procedure or administrative procedure relating to the assets of a debtor will be suspended at commencement of the corporate reorganisation procedure.

Under the Corporate Reorganisation Law, even claims secured by a special preferential right, pledge, mortgage, lien under the Commercial Code or any other security interests, such as security by way of transfer, existing over the assets of the debtor, cannot be exercised outside the procedure. A creditor may, however, execute a right of set-off until the expiration of the claim filing period if a creditor owes a debt to a debtor at the time the procedure commences.

### **Involuntary reorganisations**

#### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

##### **Civil rehabilitation procedure**

If there is a significant likelihood that a bankruptcy event will occur (see question 9 for a list of bankruptcy events), a creditor may also file a civil rehabilitation petition. A fee (¥10,000) and a deposit, determined by the court, must be paid by the creditor filing the petition to cover the costs of the procedure. A creditor must also prove prima facie to the court that the grounds for civil rehabilitation exist and must establish that it has a valid claim against a debtor.

Other aspects of the subsequent process are the same as the voluntary civil rehabilitation.

##### **Corporate reorganisation procedure**

If there is a significant likelihood that a bankruptcy event will occur (see question 9 for a list of bankruptcy events), a petition to begin a corporate reorganisation procedure may be filed by a creditor whose claim amounts to 10 per cent or more of the debtor company's paid-up capital or a shareholder that holds voting rights equal to 10 per cent or more of the total voting rights of the debtor company. A fee (¥20,000) and a deposit, determined by the court, must be paid to cover the costs of

the procedure. A creditor or shareholder must not only prove prima facie to the court that grounds for the corporate reorganisation exist but must also inform the court, with respect to a creditor, of the value of its claims, and with respect to a shareholder, of the size of its voting rights.

Other aspects of the subsequent process are the same as voluntary corporate reorganisation.

### **Mandatory commencement of insolvency proceedings**

#### **13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

If a joint-stock company is already in liquidation and a liquidator discovers that the company's debts are likely to exceed its assets, he or she is required to make a petition for the commencement of the special liquidation procedure. If the liquidator fails to do so, he can be fined up to ¥1 million.

If a company takes certain actions to carry on business after it suspended payments, the trustee-in-bankruptcy appointed by the court in the following bankruptcy procedure can annul certain acts of the company (eg, granting security to specific creditors) that would jeopardise the interests of its creditors. Almost all the same measures may be taken by the administrator or supervisor in a civil rehabilitation procedure or the administrator in a corporate reorganisation procedure, but do not apply in the case of a special liquidation procedure.

### **Doing business in reorganisations**

#### **14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

Under the civil rehabilitation procedure, the directors of a debtor company may continue to operate the business. In a corporate reorganisation, an administrator is always appointed and immediately assumes responsibility for the operation of the business.

Under both the civil rehabilitation procedure and the corporate reorganisation procedure, a debtor or an administrator may deal with the company's assets (including to sell such assets) in the ordinary course of business, unless such activities are restricted by the court (eg, office lease fee, small amount payments such as less than ¥100,000 would not be restricted). The claims of the creditor that supplies goods or services after the commencement of the procedure are regarded as 'common benefit claims' that may be satisfied at any time outside the insolvency procedure.

Under the civil rehabilitation procedure, even though a debtor or the directors of the debtor company continue to operate the debtor's business, the court can appoint an investigator (to investigate the debtor's assets), a supervisor (to approve certain activities as specified by the court) or an administrator (to take the place of the debtor or the directors of the debtor company). Under the civil rehabilitation procedure, a supervisor is appointed in most cases, but an administrator is only appointed in exceptional circumstances.

In certain circumstances it is possible for creditors (including secured parties) or shareholders to call a joint meeting to supervise the debtor's business. Under the civil rehabilitation procedure, a creditor that holds 10 per cent or more of the total amount of identified claims against a debtor or a committee of creditors (see question 26), as well as the court or the debtor, can call a creditors' meeting. Under the corporate reorganisation procedure, a committee of creditors, secured parties or shareholders, a creditor whose claim amounts to 10 per cent or more of the claims registered against the debtor company or a shareholder holding voting rights equal to 10 per cent or more of the total voting rights of the debtor company, as well as the court or an administrator, can call an affiliates' meeting (equivalent to a creditors' meeting in the civil rehabilitation procedure).

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**Stays of proceedings and moratoria**


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**15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

Since the purpose of liquidation procedures is to liquidate a debtor's assets for impartial distribution to all creditors, it is important to preserve the debtor's assets and prevent creditors from freely exercising their rights. Under the bankruptcy procedure and the special liquidation procedure, the court may grant an injunction prior to the commencement of the procedure to preserve the assets and to prevent the exercise of unsecured rights. Once the liquidation procedure has commenced, compulsory execution or other enforcement of unsecured rights are prohibited. Nevertheless, holders of a special preferential right, a pledge, a mortgage, a lien under the Commercial Code or other security rights, such as security by way of transfer, are able to exercise those rights outside the bankruptcy procedure and the special liquidation procedure (ie, the debtor's assets subject to these preferential rights are not captured within the bankruptcy procedure and the special liquidation procedure).

Under reorganisation procedures, the primary goal is to keep the business in operation with a view to rehabilitating it. The exercise of claims is, therefore, strictly limited and the court may order the discontinuance of not only executions of unsecured rights but also enforcement of security prior to the commencement of the procedure. While the civil rehabilitation procedure allows a creditor to exercise claims secured by a special preferential right, a pledge, a mortgage, a lien under the Commercial Code or other security rights, such as security by way of transfer, outside the procedure, the corporate reorganisation procedure does not.

A creditor may appeal against an order of the court for the discontinuance of unsecured and secured rights and the court may alter or withdraw the order at its discretion.

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**Post-filing credit**


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**16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**
**Liquidation**

Under the bankruptcy procedure, with the approval of the court, a trustee in bankruptcy may borrow money on behalf of the debtor only if it is necessary for the preservation and management of the debtor's assets. Such a loan or provision of credit is treated as a common benefit claim (ie, claim arising for the common benefit of all creditors such as the fees of the supervisor that has priority over general unsecured claims) that will be paid to the creditor in full when it becomes due in priority to other general unsecured creditors' claims.

**Reorganisation**

Under the civil rehabilitation and corporate reorganisation procedures, a debtor (or an administrator on behalf of the debtor) can borrow money to continue the debtor's business even after the commencement of the relevant procedure. At the time of ordering the civil rehabilitation or corporate reorganisation procedure, the court may require a debtor or an administrator to seek its prior approval for any borrowing. A claim against the debtor during a reorganisation is treated as a common benefit claim that will be paid to the creditor in full when it becomes due. Even after the civil rehabilitation or corporate reorganisation procedures are converted into a bankruptcy procedure, these claims will be treated as common benefit claims that have priority over general unsecured claims.

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**Set-off and netting**


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**17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**
**Set-off**

Under the bankruptcy procedure and the special liquidation procedure, if a creditor owes a debt to a debtor at the time of the commencement of the procedure, the creditor may set off that debt against its claims against the debtor at any time prior to completion of the procedure.

Under the civil rehabilitation procedure and corporate reorganisation procedure, a creditor can set off a debt it owes to a debtor against its claim if it was owed the debt at the time of the commencement of the procedure; and the claim becomes due before the expiration of the claim filing period (see question 23).

Under any of the liquidation and reorganisation procedures, there are two situations in which a creditor may not exercise a right of set-off. The first is when a creditor assumed a debt:

- (i) after the commencement of the insolvency proceedings;
- (ii) by executing a contract regarding the disposal of the debtor's assets mainly for the purpose of set-off or by assuming a debt owed to the debtor, and with the knowledge that the debtor is unable to pay its debts;
- (iii) with the knowledge that there had been a suspension of payments (except where the debtor was not unable to pay when there had been a suspension of payments); or
- (iv) with the knowledge that a petition for insolvency had been made.

Note that (ii), (iii) and (iv) will not apply if the debt arose by operation of the law, on grounds that existed before the creditor obtained knowledge of the debtor's inability to pay its debts, the suspension of payment or the fact that the petition of insolvency has been made, or on grounds that existed not less than one year before the petition for the commencement of insolvency proceedings was made.

The second situation in which a creditor may not exercise a right of set-off is when a person who owes a debt to the debtor acquired a claim:

- (i) from a third party following the commencement of the insolvency proceedings;
- (ii) with the knowledge that the debtor was unable to pay its debts;
- (iii) with the knowledge that there had been a suspension of payments (except where the debtor was not unable to pay when there had been a suspension of payments); or
- (iv) with the knowledge that a petition for insolvency had been made;

Note that (ii), (iii) and (iv) above will not apply if the claim arose by operation of the law, on grounds that existed before the person who owes the debt to the debtor obtained knowledge of the debtor's inability to pay its debts, the suspension of payment or the fact that a petition for insolvency had been made, or on grounds that existed not less than one year before the petition for the commencement of insolvency proceedings was made, or by an agreement with the debtor.

**Netting**

A close-out netting clause set out in a master agreement in respect of instruments traded by reference to market prices is effective in Japan and the balance as a result of netting will be recognised as a single claim under relevant insolvency proceedings.

Even if no close-out netting clause exists, a contract in respect of instruments that is not due on the commencement of insolvency proceedings will be automatically terminated and netted out if the instruments are traded by reference to market prices and the purpose of the contract cannot be achieved unless the obligations are performed on a specific date or within a certain period.

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**Sale of assets**


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**18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

Under the civil rehabilitation procedure, a debtor must obtain the approval of the court to transfer the whole or a material part of its business. The court may approve the transaction only if it is necessary for rehabilitation or reorganisation of the business. However, if the court has approved a rehabilitation plan that includes a business transfer, the debtor is not required to obtain additional court approval for that business transfer. The court may, if necessary, order that the debtor or administrator must obtain court consent to sell specific assets of the debtor.

Under the corporate reorganisation procedure, a business transfer will be made in compliance with the reorganisation plan. Before completion of the reorganisation plan, an administrator may transfer the whole or a material part of the business with the approval of the court. The court may, if necessary, order that the administrator must obtain court consent to sell specific assets of the debtor.

Under both the bankruptcy procedure and the special liquidation procedure, a business transfer and a sale of specific assets require the approval of the court unless otherwise stated in applicable laws.

In theory, the sale of assets under insolvency proceedings does not automatically release the assets from the secured interests over them. However, in practice, a debtor or an administrator will contact the secured parties and negotiate the price to be paid to them in consideration for the release of the assets. If the negotiation is successful, the assets will be sold free and clear of claims and liabilities. If one or more of the secured parties (typically lower-ranked secured parties who cannot expect any distribution) do not agree to a release of their security interests, then the debtor or the administrator may consider a petition for the extinction of such security interests. Under the Bankruptcy Law, the Civil Rehabilitation Law and the Corporate Reorganisation Law, the court may order the extinction of security interests over assets of a debtor subject to certain conditions. If the security interests are declared to be released, the assets can be sold free and clear from the claims (see question 32 for further details).

Even if an interim agreement is being negotiated for a business transfer, or sale and purchase of any assets of the debtor, the debtor or the administrator may continue to seek better terms from other parties.

Creditors are not allowed to set off their claim against a debt that was incurred after the commencement of the procedures by the creditors. Therefore, a creditor seeking to purchase the assets or business of the debtor during the bankruptcy, civil rehabilitation, corporate reorganisation or special liquidation procedures is not permitted to pay the purchase price by reducing the amount of its claim against the debtor. Accordingly credit bidding is not permitted in Japanese insolvency proceedings.

### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

The licensor or owner of IP cannot terminate the debtor's right to use it because of the commencement of insolvency procedures. A clause in an IP licence providing for a right of termination on insolvency is considered to be void. Under the Bankruptcy Law, Civil Rehabilitation Law and the Corporate Reorganisation Law, the administrator or debtor can either choose to terminate the licence contract or to pay the licence fee and continue to use the IP rights.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Personal Information Protection Act (the PIPA) prohibits a company from transferring personal data (as defined in the PIPA) to a third party without the consent from the person relevant to the personal data. The exemptions from this rule will apply when the company transfers personal data to a third party 'in accordance with' the statutory laws or in the course of business transfer such as statutory merger. Thus a company can rely on one of these exemptions when it contemplates to use personal data in the insolvency process in accordance with applicable insolvency laws (eg, disclosure to an administrator) or to transfer personal data to a purchaser of its business as a result of the applicable insolvency procedure.

### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

Under both the civil rehabilitation procedure and corporate reorganisation procedure, a debtor or an administrator may choose whether or not to cancel an agreement with bilateral obligations (ie, including ordinary sales and purchase agreements but not an agreement with unilateral obligation) if neither party (ie, neither the debtor or the creditor) has completed the performance of its obligations by the time of the commencement of rehabilitation proceedings or corporate reorganisation proceedings. Therefore, if the agreement is not bilateral or if either the debtor or the creditor has already performed their obligations by the time of the commencement of the relevant insolvency proceedings, the debtor or the administrator may not decline to perform their obligations under such agreement. However, the debtor or the administrator cannot terminate a lease or licence agreement with which a lessee or licensee has perfected its rights against third parties (eg, registration of the building subject to the relevant land lease under the Act on Land and Building Leases).

Under the civil rehabilitation procedure, at the time of ordering the civil rehabilitation procedure the court may order that the debtor or the administrator must obtain consent from the court when the debtor or the administrator cancels agreements with unperformed bilateral obligations. Similarly, under the corporate reorganisation procedure, the administrator may be required by the court to obtain consent from the court to cancel agreements with unperformed obligations. If agreements with unperformed bilateral obligations are cancelled, a creditor's claims for damages arising from such cancellation will be regarded as unsecured claims in both civil rehabilitation and corporate reorganisation proceedings.

Under both the civil rehabilitation procedure and corporate reorganisation procedure, when a debtor fails to pay to a creditor after the civil rehabilitation procedure or corporate reorganisation procedure is commenced, the failure to pay would not constitute breach of contract under Japanese contract law which could trigger the statutory right to terminate the relevant contract. On the other hand, the creditor may terminate a contract with the debtor on the basis of the contractual clause under which the creditor is entitled to terminate the relevant contract as a result of the commencement of such insolvency procedure, so long as the contractual clause is not connected with the debtor's failure to pay because of an insolvency event.

### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Arbitration is rarely used in Japan (both with respect to insolvency proceedings and other areas of law), although there is no particular limitation on the availability of arbitration in insolvency cases. Although it is not clear from the law, it is generally considered that an arbitration proceeding can be continued after an insolvency procedure is commenced. It is also the prevailing opinion that an arbitration agreement will be binding even after an insolvency procedure is commenced, and thus creditors can apply for the commencement of an arbitration procedure based on an existing arbitration clause. To agree to submit certain disputes to arbitrators and to abide by their arbitral award, an administrator in a bankruptcy procedure and a liquidator in a special liquidation procedure require permission from the court. Under the civil rehabilitation procedure and corporate reorganisation procedure, the court may order that debtors or administrators request the court's permission to conclude such an arbitration agreement.

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**Successful reorganisations**


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**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**
**Civil rehabilitation**

After expiration of the period for filing claims (see question 31), the debtor or administrator must prepare a civil rehabilitation plan and submit it to the court within the period prescribed by the court. The plan must be viable and fair as between the creditors of each separate class. Under the civil rehabilitation procedure, creditors' claims are divided into four categories: secured interests of certain types over a particular asset (eg, special preferential right, pledge, mortgage, lien under the Commercial Code, or any other security interests, such as security by way of transfer); preferred claims (such as unpaid wages or tax payments); unsecured claims; and common benefit claims (claims arising for the common benefit of all creditors such as the fees of the supervisor and any necessary running costs incurred following the commencement of civil rehabilitation) that are excluded from the civil rehabilitation procedure and are paid in full when they become due. Secured interests over a particular asset of the debtor will be exercised outside the civil rehabilitation procedure and only the shortfall will be treated as unsecured claims under the civil rehabilitation procedure.

Following submission of the civil rehabilitation plan, the court will convene a creditors' meeting where the plan is discussed by the creditors, except where the court decides not to hold a meeting and allow creditors to vote by post instead. The civil rehabilitation plan will be subject to the approval of a simple majority of the creditors present at the meeting or, as the case may be, a simple majority of the creditors who exercise their voting rights by post and a majority of the creditors who represent between them at least half of all allowed creditors' claims. Once the civil rehabilitation plan has been approved by the creditors, the debtor or administrator will seek the court's approval of the plan. Upon the approval of the court, the rights of all creditors and shareholders are modified in accordance with the civil rehabilitation plan.

The rehabilitation plan can modify some or all of the rights of 'creditors', if approved, but it cannot release non-debtor parties (ie, directors, accounting advisers, statutory auditors, executive officers, accounting auditors or lenders) from their liabilities. However, the debtor or the administrator may, during the course of the civil rehabilitation procedure and outside the rehabilitation plan, release those parties from all or part of their liability by following the procedures set out in the Companies Act, such as obtaining unanimous shareholders' approval and the permission of the court for waiver of the claims.

**Corporate reorganisation**

As under the civil rehabilitation procedure, the corporate reorganisation plan will be prepared and submitted to the court by the administrator within the period prescribed by the court after expiration of the period for filing claims. The plan must be viable and fair as between the creditors or shareholders of each separate class. Under the corporate reorganisation procedure, creditors' claims are divided into four categories: secured interests of certain types (a special preferential right, a pledge, a mortgage, a lien under the Commercial Code, or any other security interests, such as a security by transfer) over a particular asset of the debtor; preferred claims; unsecured claims; and common benefit claims. Secured claims cannot be exercised outside the corporate reorganisation procedure.

Following submission of the corporate reorganisation plan, the court will convene meetings for each class of creditors and shareholders to discuss the plan, except where the court decides not to hold a meeting and allow creditors and shareholders to vote by post instead. The reorganisation plan must be approved by each class of creditors and shareholders, as follows:

- if the plan only extends the due date of secured claims, the approval of the secured creditors representing two-thirds of all allowed secured claims (by value) is required;
- if the plan does more than just extend the due date of secured claims, the approval of three-quarters of all allowed secured claims (by value) is required; and

- if the plan proposes the abolition of the whole business of the debtor, then the approval of nine-tenths of all allowed secured claims (by value) is required.

The reorganisation plan will be subject to the approval of a simple majority of the unsecured creditors that represent between them at least half of allowed unsecured creditors' claims (by value). The reorganisation plan must be approved by a simple majority of shareholders that hold a majority of total voting rights in the debtor. Once the reorganisation plan has been duly approved by the creditors and shareholders, the administrator will seek the court's approval of the plan. Upon approval by the court, the rights of all creditors and shareholders will be modified in accordance with the reorganisation plan.

As with the civil rehabilitation procedure, the reorganisation plan can modify some or all of the rights of creditors, if approved, but it cannot release non-debtor parties. However, the debtor or the administrator may release those parties outside the reorganisation procedure.

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**Expedited reorganisations**


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**24 Do procedures exist for expedited reorganisations?**

The civil rehabilitation procedure includes two types of simplified reorganisation procedures to expedite a reorganisation. One is the simplified civil rehabilitation procedure, in which there is no investigation of claims against the debtor. This procedure may be started after the expiration of the period for filing claims (see question 29) with the approval of creditors who represent between them at least three-fifths (as determined by the court) of all creditors' claims (by value). The second is an agreed rehabilitation procedure, in which there is no investigation of claims against the debtor or approval of a civil rehabilitation plan in a creditors' meeting. The agreed rehabilitation procedure may be started after the expiration of the period for filing claims with the approval of all of the creditors and the court.

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**Unsuccessful reorganisations**


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**25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**
**Civil rehabilitation**

The civil rehabilitation plan may be rejected either by disapproval of the plan at a creditors' meeting or by the court's decision after creditor approval at the meeting. If a proposed civil rehabilitation plan is not approved by the majority of creditors or by the court itself, the court will order the termination of the civil rehabilitation procedure and may order the commencement of bankruptcy procedures. If the debtor fails to perform its obligations under an approved plan, the creditor may enforce its claim against the debtor.

The court may also annul the plan following a petition by a creditor who holds a claim against the debtor equal to or more than 10 per cent of the remaining debt obligations of the debtor set out in the plan, if the plan was approved in an unjustifiable way (eg, creditors' approval has been obtained through fraudulent means), the debtor failed to perform the plan, or the debtor was in violation of restrictions ordered by the court. The court may abolish the plan by its own decision if the debtor was in violation of restrictions ordered by the court or it is unlikely that the plan will be successfully performed. On annulment or abolishment of the plan by the court, the rights of all creditors and shareholders will be restored to their state before they were modified in accordance with the rehabilitation plan.

**Corporate reorganisation**

The corporate reorganisation plan may only be formally rejected by the court following meetings of creditors and shareholders to discuss the plan. If the corporate reorganisation plan is not accepted by the creditors or the shareholders, the court may force the creditors or shareholders to accept the plan by amending it to protect the interests of dissenting creditors or shareholders. If the court rejects the corporate reorganisation plan, the court will order the termination of the corporate reorganisation procedure and may order the commencement of bankruptcy procedures. Even after the court has approved a corporate reorganisation plan, it may abolish the plan by its own decision if it is unlikely that the plan will be successfully performed. Even on such abolishment of

the plan by the court, the rights of all creditors and shareholders will remain as modified in accordance with the reorganisation plan.

### Insolvency processes

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

#### Notices given to creditors

When any of the insolvency proceedings are commenced, a notice is sent to all creditors known to the debtor and a public notice is posted in the courthouse and in the official gazette. Throughout the insolvency proceeding, all creditors who have submitted a claim must be notified of any creditors' meetings that are to be convened (with some limited exceptions).

#### Creditors' meetings

Under Japanese insolvency law, a court or, in the case of a special liquidation procedure, a liquidating company, must convene a 'creditors' meeting' in certain circumstances.

In relation to the bankruptcy procedure, a creditors' meeting does not have to be held, however, the court will convene a meeting under certain circumstances, including at the request of either the trustee-in-bankruptcy, the creditors' committee or certain of the creditors or if the court deems it necessary.

Usually, an initial creditors' meeting is held on a date decided by the court. In the meeting, the trustee-in-bankruptcy reports to the creditors:

- the financial status of the debtor;
- the reasons for bankruptcy;
- whether there are any circumstances that require a court order to assess the liabilities of the officers of the debtor or a court order to freeze the officers' assets; and
- any other matters necessary for the bankruptcy procedure.

Furthermore, after all distributions to creditors have been made, the trustee-in-bankruptcy shall give an accounting report either at a creditors' meeting or in writing. Under the special liquidation procedure, a creditors' meeting will be held when the liquidator deems it necessary. Creditors whose claims represent 10 per cent or more of the total claims (by value) can ask the liquidator to hold a creditors' meeting.

In the civil rehabilitation and corporate reorganisation procedures, a creditors' meeting is not necessarily held. In the civil rehabilitation procedure, the court will convene a meeting at the request of the debtor or administrator, creditors' committee or creditors who hold claims against the debtor equal to 10 per cent or more of the amount of claims of all creditors.

In the corporate reorganisation procedure, the court will convene a meeting at the request of the administrator, relevant committees (committees of unsecured creditors, secured creditors and shareholders), creditors that hold claims against the debtor equal to 10 per cent or more of the amount of claims of all creditors that reported their debt to the debtor or shareholders who hold voting rights equal to 10 per cent or more of the voting rights of total shareholders.

In both civil rehabilitation and corporate reorganisation procedures, the court may convene a meeting if it determines a creditors' meeting necessary. Usually, an initial creditors' meeting is held at which the administrator reports the financial status of the debtor to its creditors and the creditors state their opinion as to the suitability of the administrator, the business and the management of the debtor's assets. Following the submission of the civil rehabilitation or corporate reorganisation plan, the court may convene a creditors' meeting (in the case of the corporate reorganisation procedure, such a meeting may also be attended by the shareholders) to discuss the plan except where the court decides not to hold a meeting and allows creditors and shareholders, if applicable, to vote by post instead.

A reorganisation plan cannot provide for the release of liabilities owed by third parties who are not part of the debtor group subject to the reorganisation plan.

### Committees

In relation to the bankruptcy and civil rehabilitation procedures, creditors may form a creditors' committee. In the corporate reorganisation procedure, secured creditors, unsecured creditors and shareholders may form a secured creditors' committee, an unsecured creditors' committee or a shareholders' committee respectively. See question 28 for further details of these committees.

Information available to the creditors or creditors' committees and reporting obligations of insolvency administrators

In the bankruptcy procedure, the trustee-in-bankruptcy must, immediately after the commencement of the procedure, submit to the court and the creditors' committee (if one exists), an inventory of the debtor's property and the debtor's balance sheet together with a report outlining:

- the financial status of the debtor;
- the reasons why the debtor became bankrupt;
- whether circumstances require a court order to assess the liabilities of the officers of the debtor or a court order to freeze the officers' assets; and
- any other matters necessary for the bankruptcy procedure.

If a creditors' meeting is held, the trustee-in-bankruptcy must summarise the contents of the above report to the creditors at the creditors' meeting. If a creditors' meeting is not held, the trustee-in-bankruptcy must provide the creditors who are known to the trustee-in-bankruptcy with a summary of the above report. In addition, the trustee-in-bankruptcy must report to the court the status of the administration and disposition of the debtor's property together with any other matters requested by the court. The trustee-in-bankruptcy must also report the status of the debtor's property to the creditors' meeting upon a resolution of the creditors' meeting. The trustee-in-bankruptcy shall, upon the termination of his or her office, give an accounting report either at a creditors' meeting or in writing.

If the creditors' committee requests, or a resolution of the creditors' meeting is made, the debtor and its related parties, such as any representatives, directors or statutory auditors, must provide necessary explanations concerning the bankruptcy to the creditors. The creditors may, under certain circumstances, ask the court to ensure the disclosure and copying of any documents (or other objects) that have been prepared by the court or submitted to the court by the trustee-in-bankruptcy or any other persons (such as the debtor).

In the civil rehabilitation procedure, the debtor or the administrator (if one has been appointed) must, immediately after the commencement of the procedure, submit to the court and the creditors' committee (if one exists), an inventory of the debtor's property and the debtor's balance sheet together with a report on:

- the reasons why the debtor became insolvent;
- the past and present status of the business and assets of the debtor;
- whether circumstances require a court order to assess the liabilities of the officers of the debtor or a court order to freeze the officers' assets; and
- any other matters necessary for the civil rehabilitation procedure.

The debtor or, if an administrator has been appointed, the administrator, usually holds a briefing session for all the creditors immediately after the commencement of the procedure outlining the issues to be explained in the above report, together with any other material issues for the procedure in general. The debtor or the administrator (if one has been appointed) must also report to the court the status of the business and property of the debtor and any other matters requested by the court.

In the corporate reorganisation procedure, the administrator, immediately after the commencement of the procedure, must submit to the court and the creditors' committee (if one exists), the inventory of the debtor's property and the debtor's balance sheet together with a report describing:

- the reasons why the debtor became insolvent;
- the past and present status of the assets and the business of the debtor;
- whether circumstances require a court order to assess the liabilities of the officers of the debtor or a court order to freeze the officers' assets; and
- any other matters necessary for the corporate reorganisation procedure.

The administrator has to:

- hold a briefing session for the creditors and other interested parties (such as shareholders) and summarise the content of the above report;
- deliver the summary of the report to the creditors and other interested parties by other methods; or
- take any other appropriate measures. The administrator must also report to the court the status of the business and property of the debtor and any other matters requested by the court.

In the civil rehabilitation and corporate reorganisation procedures, if the debtor or the administrator intends to transfer its business to a third party and asks a court for approval of the transfer (see question 18), the court has to explain the transfer to the creditors who are known to the court and hear opinions from them before the court approves such a transfer. In addition, prior to a creditors' resolution for a rehabilitation plan or a reorganisation plan, the court must send a draft rehabilitation or reorganisation plan (together with related documents) to the creditors and, if necessary, hold a briefing session to explain the plan to the creditors. The creditors may, under certain circumstances, ask the court to ensure the disclosure and copying of any documents (or other objects) that have been prepared by the court or submitted to the court by the debtor or any other persons (such as the administrator). The administrator will, upon the termination of his or her office, give an accounting report to the court.

In the special liquidation procedure, when the liquidator has completed the investigations into the current status of the liquidating company's property and prepared an inventory of the liquidating company's property and balance sheet, the liquidating company must submit them to the court without delay. The liquidating company also has to report to the creditors the outcome of such investigations and summarise the inventory of the property and balance sheet. It must state its opinions on the prospects of the liquidation procedure (and its implementation) at a creditors' meeting, or by any other appropriate means. The creditors may, under certain circumstances, ask the court to ensure the disclosure and copying of any documents (or other objects) that have been prepared by the court or submitted to the court by the liquidating company (or any other persons). In addition, whenever a creditors' meeting is to be held, the person calling the meeting must provide the creditors known to him or her with necessary materials so that the creditors are informed when they exercise their voting rights.

#### Remedies against third parties

In all the insolvency proceedings, creditors may not initiate proceedings to pursue remedies against third parties. Only a trustee or administrator may initiate such proceedings.

#### Enforcement of estate's rights

##### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Under the bankruptcy procedure, the civil rehabilitation procedure and the corporate reorganisation procedure, the right to pursue a claim for the benefit of the estate belongs solely to the insolvency administrator. The creditors cannot pursue the estate's remedies, which the debtor possesses. The creditors may only claim damages if the insolvency administrator neglects to pursue a claim.

#### Creditor representation

##### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

In relation to the bankruptcy and civil rehabilitation procedures, creditors may form a creditors' committee. Under the corporate reorganisation procedure, secured creditors, unsecured creditors and shareholders may form a secured creditors' committee, an unsecured creditors' committee or a shareholders' committee respectively. As such committees are voluntarily formed, there are no regulations regarding the selection and the appointment of the members of the committees. Such committees may participate in the relevant procedures if the court approves. The court may give such approval only if:

- the number of the committee members is between three and 10;
- a majority of the creditors that have submitted claims (or, in the case of the shareholders' committee, a majority of the shareholders) consent to the committee's participation in the procedure; and
- the committee fairly represents the interests of all creditors (or, in the case of the shareholders' committee, the interests of all shareholders). The committees are not prohibited from retaining advisers.

Each committee is given certain powers, which include the right:

- to state its opinion to the court, the debtor or the administrator regarding the procedure;
- to convene creditors' meetings; and
- to supervise the implementation of the procedure.

If a committee has contributed to the smooth progress of bankruptcy proceedings or the rehabilitation or reorganisation of the debtor, and has incurred necessary expenses for such activities, the court may, following a creditor's petition (or, in the case of a shareholders' committee, a shareholder) permit reimbursement of any reasonable expenses, from the property of the debtor.

In the special liquidation procedure, there are no provisions regarding a creditors' committee.

#### Insolvency of corporate groups

##### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

As set out in question 2, insolvency proceedings by the parent and its subsidiaries can be combined for administrative purposes. However, there are no procedures that combine the assets and liabilities of these companies into one pool and transfer assets from an administration in Japan to an administration in another country. As a general rule, it is argued that creditors may submit their claims not only against a debtor, but also where it is deemed appropriate to pierce the corporate veil against that debtor's parent or subsidiaries.

#### Appeals

##### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Statutory rights of *sokuji koukoku* (immediate appeal) of certain court orders will be available to a person who has statutory interest to the relevant court order. For example, if a creditor applies for the commencement of a bankruptcy process, civil rehabilitation process, corporate reorganisation process or special liquidation process and a competent court admits the application and issues the commencement order, a relevant debtor/company can file an immediate appeal with the court. These rights of appeal are automatic rights, and no permission or posting security will be required.

#### Claims

##### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

In bankruptcy, civil rehabilitation and corporate reorganisation procedures, the court decides and publicly announces the period for filing claims (which must be between two weeks and four months in duration), during which creditors must file their claims against the debtor with the court to be able to participate in the proceedings.

When filing its claim, a creditor is required to report prescribed matters, such as the amount and basis of the claim and whether any

right of priority exists. After expiration of the period for filing claims, the court clerk will prepare a claim chart listing all claims filed with the court and the claims that are subject to examination.

If a creditor's claim is disputed by the debtor, the trustee-in-bankruptcy, the administrator or any other creditor, the creditor may initiate legal action against the person objecting to the claim. If no objection has arisen with respect to a claim at a creditors' meeting or within the claim examination period, the amount and priority of the claim will be finalised. In relation to the special liquidation procedures, creditors (except those already known to the debtor) must submit their claims to the liquidator. There is no specific provision regarding how to submit a claim, which claims may be disallowed or what action the creditor should take to challenge a disallowance.

Under the Bankruptcy Law, the Civil Rehabilitation Law and the Corporate Reorganisation Law, a creditor that acquires a claim that has been filed with the court is required to inform the court that it has acquired the claim to participate in the proceedings. The creditor can claim the claim's full face value via the insolvency proceedings even when the claim has been acquired by the creditor at a discount. There are no other restrictions on the transfer of either claims or transferred claims.

Under the Bankruptcy Law, the Civil Rehabilitation Law and the Corporate Reorganisation Law, claims for contingent or unliquidated amounts are recognised. Claims for contingent or unliquidated amounts must be provisionally calculated as of the commencement of the proceedings, and the actual amounts will be determined within the applicable proceedings. A creditor is free to claim interest that accrued after the opening of any of bankruptcy, civil rehabilitation and corporate reorganisation procedures. However, such claim are subordinated to other claims by operation of laws (see question 38) and therefore, practically the creditor cannot expect to receive any distribution on that claim.

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#### Modifying creditors' rights

##### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

As a general rule, the court cannot change the rank of a creditor's claim, which is stipulated under the law. However, under the Bankruptcy Law, the Civil Rehabilitation Law and the Corporate Reorganisation Law, the court has the right to give permission for the release of security rights. Under the Bankruptcy Law, the court can approve the release of a security right by the administrator, who can then sell the relevant property and pay the relevant amount to the holder of the security right, if this is in the general interests of all of the creditors. Under the Civil Rehabilitation Law, if a property is indispensable for the continuation of the debtor's business, the court can approve that the relevant security rights are released by making the debtor (or the administrator, if appointed) pay the price of such property to the court and distributing it to the security holders. Under the Corporate Reorganisation Law, when it is necessary for the reorganisation, the court can approve that security rights are released by making the administrator pay the price of such property to the court.

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#### Priority claims

##### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

There are no governmental or non-governmental privileged and priority claims in any of the insolvency proceedings, except for taxation payments, which are treated preferentially in insolvency proceedings. Claims given priority in the law and claims arising for the common benefit of all creditors (such as the fees for the trustee or administrator and any necessary running costs incurred following the commencement of the proceeding) are treated as 'common benefit claims' and have priority over other claims. The common benefit claims are paid in full when they become due.

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#### Employment-related liabilities in restructurings

##### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

If a company has to terminate the employment of the employees during a restructuring or liquidation, it must follow the rules under the Labour Standard Act and the Labour Contract Act. In order to legally terminate the employment:

- a company has to give at least 30 days' prior notice to an employee or pay at least 30 days' salary to the employee in lieu of notice; and
- there must be objective and reasonable grounds for the termination and such termination must be socially acceptable (eg, where the employee is performing at a consistently low level in carrying out his or her duties and the employer can prove that improvement of his or her performance is unlikely even if additional training is provided).

In the context of restructuring or downsizing, the following four factors will generally be considered by the court in determining the reasonableness of termination:

- the necessity to reduce personnel (economic condition of the company);
- the necessity to terminate employees in order to reduce the number of personnel (possibility of job rotation or voluntary resignation);
- the fairness of the standards used for selecting the particular employees whose employment is being terminated; and
- procedural fairness.

Employees whose employment has been terminated can bring claims to have their jobs reinstated and to be paid unpaid wages by arguing that the termination did not satisfy the conditions set out above and is therefore void. Where large numbers of employment contracts are terminated or where the business ceases operations, it is likely that they will cooperate through a trade union and as a result the number of employee claims is likely to increase. If the termination were found to be invalid, the company would have to pay unpaid wages (past and future wages). If the termination were found to be valid, the company would have to pay unpaid wages and retirement allowance (where applicable).

Unpaid wages and retirement allowance including pension have certain priorities in restructuring or liquidation proceedings. If there exist deficiencies in pension plans or schemes, employees will have claims against the company with certain priorities.

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#### Pension claims

##### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

In Japan employees have pension-related claims against an entity (often a trust), which is segregated from the employers' and managers' pension assets. Accordingly, the employer's insolvency does not affect such claims, although it may affect the membership of any pension funds in which the employee has participated.

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#### Environmental problems and liabilities

##### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The insolvency administrator (in a bankruptcy procedure and a corporate reorganisation procedure) or the debtor (in a civil rehabilitation procedure) is primarily responsible for dealing with the environmental issues identified during the relevant insolvency procedures. Thus secured or unsecured creditors, or third parties do not have any liability for such environmental issues, unless they have agreed to bear certain costs to remedy the damage caused. Generally, the insolvency administrator or the debtor is expected to closely discuss with the insolvency court how the identified environmental issue (eg, land pollution) can

be cleaned up during the insolvency procedure and to try to remedy it on the debtor's account as much as possible.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

In a civil rehabilitation procedure, once the rehabilitation plan is finally approved by the court, the debtor will be discharged from every unsecured claim other than claims approved by the rehabilitation plan, claims that have not been filed within the filing period because of grounds not attributable to the relevant creditors or certain other liabilities set out in the Civil Rehabilitation Law. Common benefit claims, preferred claims, secured interests of certain types (special preferential rights, mortgage, lien under the Commercial Code, or any other security interest, such as security by way of transfer) will survive the rehabilitation procedure.

In a corporate reorganisation procedure, once the reorganisation plan is approved by the court, the debtor will be discharged from every secured and unsecured claim other than claims approved by the reorganisation plan, claims for retirement benefits of the debtor's officer (such as directors, auditors, representative directors and executive officers) and the debtor's employees who took office or were employed after the commencement of the reorganisation procedure or certain other liabilities set out in the Corporate Reorganisation Law. Common benefits claims will survive the rehabilitation procedure.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In the bankruptcy procedure, distributions to creditors will be made after the permission of the court clerk is obtained. A distribution will be made each time the trustee-in-bankruptcy receives sufficient funds to be distributed by liquidating the debtor's assets. A creditor that has a secured interest over a particular asset of the debtor may enforce such interest outside the bankruptcy proceedings. Other claims are paid in the following order of priority as calculated by the trustee-in-bankruptcy and approved by the supervisors (if they are appointed) or by the court:

- common benefit claims (including tax);
- preferred claims (such as unpaid wages);
- unsecured claims;
- subordinated claims (such as interest that accrued after the declaration of bankruptcy); and
- subordinated claims created by agreements.

Within each category of claim, each claim will be settled on a pro rata basis.

In the special liquidation procedure, distributions to creditors can be made by the liquidator at any time after the relevant claim is submitted to the liquidator; however, in practice, such distributions are rarely made at this stage. If the distribution plan is approved by creditors and the court, distributions to creditors will be made subject to the plan.

In relation to the civil rehabilitation and corporate reorganisation procedures, distributions to creditors will be made in accordance with the approved civil rehabilitation or corporate reorganisation plan (subordinated claims created by agreements are inferior to the ordinary unsecured claims in the plan).

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

As a general rule, if neither the debtor nor the counterparty has completely performed its obligations under an agreement with bilateral obligations, the trustee-in-bankruptcy under the bankruptcy procedure, the debtor (or the administrator, if appointed) under the civil rehabilitation procedure or the administrator under the corporate reorganisation procedure has the discretion to terminate such an agreement. However, the trustee, debtor or administrator cannot terminate a lease or licence agreement in relation to which the lessee or licensee has perfected its rights against third parties. Further, the counterparty

of the debtor with respect to a continuing supply and service agreement (eg, for electricity or gas) cannot refuse to provide that service for the reason that the debtor has not paid for it.

In the bankruptcy procedure, the following acts can be annulled by a legal action initiated by the trustee-in-bankruptcy:

- any acts of the debtor (excluding the creating of securities or dissolving of debts) that were taken with the knowledge that such actions would jeopardise the interests of its creditors;
- any acts of the debtor (excluding the creating of securities or dissolving of debts) that would jeopardise the interests of its creditors that the debtor made after it suspended payments or filed a petition of commencement of bankruptcy procedures;
- any disposal of its assets in exchange for adequate consideration by the debtor, made in circumstances where the disposal would enable the debtor to conceal or provide the proceeds free of charge or otherwise jeopardise the interest of creditors, the debtor had such an intention at the time of the transaction and the purchaser was aware of that intention of the debtor;
- any acts of the debtor (limited to creating securities or dissolving debts) that were taken after the debtor became unable to pay its debts (and the creditor had knowledge of the debtor's inability to pay its debts or suspension of payment) or after the petition for the commencement of the insolvency procedure was filed (and the creditor knew that the petition had been filed); and
- any acts of the debtor (limited to creating securities or dissolving debts) that it was under no obligation to perform or that it performed other than in accordance with its obligations, including payments made before the applicable due date, and that were made in the 30 days preceding the date on which the debtor became unable to pay its debt or later, and the creditor knew that the debtor's act would jeopardise the interests of other creditors.

Almost all the same measures may be taken by the administrator or supervisor in a civil rehabilitation procedure or the administrator in a corporate reorganisation procedure, but do not apply in the case of a special liquidation procedure.

If a transaction is annulled, the debtor's assets that were the subject of the transaction are restored to their original state.

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

There is no definition of a 'suspect period' under the bankruptcy, civil rehabilitation and corporate reorganisation procedures. However, with respect to an act that is outside the scope of the debtor's obligations (see above), the 30 days preceding the date on which the debtor suspended payments or filed a petition for the commencement of any insolvency proceeding or later, as set out in the relevant insolvency laws, can be said to function as the 'suspect period'.

Voidable transactions can only be challenged by a trustee-in-bankruptcy (in a bankruptcy procedure), a supervisor or an administrator, as appropriate (in a civil rehabilitation procedure), or an administrator (in a corporate reorganisation procedure) and only in these procedures.

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### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

There is no particular provision that makes corporate officers or directors liable for any obligations owed by their companies under insolvency procedures. However, under the Companies Act, if a corporation causes damage to a third party because of the wilful misconduct or gross negligence of its director, that director will be liable to the third party.

Under the Bankruptcy Law, the directors of the debtor will incur criminal sanctions (imprisonment for up to 10 years or a fine of up to

¥10 million, or both) if they do any of the following before or after the commencement of the bankruptcy procedure, with the intention of jeopardising the interests of the debtor's creditors:

- hide or destroy any assets of the debtor;
- disguise a disposal or a debt burden with respect to any assets of the debtor;
- change the condition of any assets of the debtor or impair its assets; or
- dispose of assets of the debtor in a manner contrary to the interests of creditors or incur obligations that are against the interests of creditors.

The directors of the debtor will also incur criminal sanctions (at the level set out above) if they obtain or make a third party obtain assets of the debtor without a trustee's approval or any other justifiable reason for the purpose of jeopardising the interests of the debtor's creditors with the knowledge that the bankruptcy procedure was commenced or other protective orders were made.

Amending, hiding or destroying financial records for the purpose of jeopardising the interests of the debtor's creditors are also criminal offences under the Bankruptcy Law (with sanctions of imprisonment for up to three years or a fine of up to ¥3 million, or both).

Breach of other duties set out in the Bankruptcy Law by a director would also result in criminal sanctions for that director. For example, a director who refuses to provide an explanation required, to accept inspections or to disclose the assets of the company, or a director who provides false explanations or information will be criminally liable under the Bankruptcy Law (imprisonment of up to three years or a fine of up to ¥3 million, or both). Also, a director who interferes with the operations of the trustee-in-bankruptcy through fraudulent means or by forcible obstructions will be subject to criminal sanctions (imprisonment for up to three years or a fine of up to ¥3 million, or both).

Similar criminal sanctions will be imposed under the civil rehabilitation or corporate reorganisation procedures, while the special liquidation procedures do not have any such sanctions.

Furthermore, if a director or officer of a debtor enters into a transaction with a third party and does not inform that third party that the debtor is insolvent or is likely to become insolvent and the third party suffers damage as a result of a subsequent insolvency, the director or officer can be punished on the basis that he or she has committed fraud under the Criminal Code (with a sanction of imprisonment for up to 10 years).

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Except for extreme cases where a parent is seen as 'abusing' the judicial personality of its subsidiary (eg, the subsidiary is used as a facade of the parent's benefit), in which case the corporate veil of the subsidiary is pierced and the parent is liable for the subsidiary's liabilities, a parent or affiliated corporation will generally not be responsible for the liabilities of subsidiaries or affiliates.

A court looks at each group company separately and cannot order a distribution of group company assets pro rata without regard to the assets of the individual corporate entities involved.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

No.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Once the insolvency proceedings have begun, a debtor's creditors are prohibited from seizing any of the debtor's assets to enforce their rights against the debtor, except where a secured creditor, holding security over a particular asset of the debtor, enforces such a security (although

in the corporate reorganisation procedure, a secured creditor cannot enforce its security).

Liquidation is generally carried out in a manner agreed by secured creditors and the debtor. Alternatively, liquidation can be in accordance with the Civil Enforcement Law, in line with the procedure applicable to the types of security in place. The cash generated by the liquidation will be paid to secured creditors to satisfy their claims and any remaining sums will be paid to the debtor, trustee or administrator for distribution to other creditors. There is no other process by which the debtor's assets may be seized and liquidated outside of the bankruptcy process or court proceedings.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Under the Companies Act, a company may be dissolved in various ways, including on the occurrence of certain trigger events set out in its articles of incorporation, by court order and by a special resolution at a shareholders' meeting to dissolve the company. After dissolution, the company will go into liquidation and all the assets of the company will be sold. A director, a person prescribed by the articles of incorporation, a person appointed at a shareholders' meeting of the company or a person appointed by the court will be appointed as liquidator and the court will supervise the liquidator. The liquidator will issue public notices and individual notices to known creditors of the dissolved company to request the submission of claims immediately after dissolution. The liquidator sells all of the debtor's assets and makes the necessary distributions to creditors who have submitted claims. Any remaining assets will be distributed to shareholders.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

The bankruptcy procedure is concluded when the court orders an end to the proceedings after a final creditors' meeting at which the trustee-in-bankruptcy reports that the final distribution of the debtor's assets to the creditors has been completed (or after the period for publication of the trustee's report has ended, if no such meeting is held).

The civil rehabilitation procedure is concluded:

- if neither a supervisor nor an administrator is appointed, when the rehabilitation plan is finalised by the court;
- if a supervisor is appointed, when the rehabilitation plan is completed or when three years have passed since the finalisation of the plan by the court; or
- if an administrator is appointed, when the rehabilitation plan is completed or when the court confirms that the rehabilitation plan will definitely be carried out.

The corporate reorganisation procedure is concluded by a declaration of the court when all the actions under the corporate reorganisation plan are completed, more than two-thirds of the claims under the plan have been paid to creditors (and there have been no defaults under the plan) or the court confirms that the corporate reorganisation plan will definitely be carried out.

Special liquidation procedures are concluded when all of the claims are paid in accordance with the agreed plan or when the need for the special liquidation procedure no longer exists.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

The Act on Recognition of and Assistance for Foreign Insolvency Proceedings (ARAFIP) sets out the requirements for recognition of

insolvency proceedings initiated outside Japan and the measures required to be taken to extend such proceedings to the debtor's assets in Japan. The Tokyo District Court, which has exclusive jurisdiction over these procedures, will, when certain requirements are met, recognise insolvency proceedings that have been commenced with respect to a debtor outside Japan and will take measures to extend the effect of such insolvency proceedings to the assets and business of a debtor in Japan. These measures include prohibiting the separate enforcement or attachment by creditors against a debtor's assets in Japan and issuing an administrative order that grants power to a court-appointed administrator to administer a debtor's assets and business in Japan.

Under the Bankruptcy Law, the Civil Rehabilitation Law and the Corporate Reorganisation Law, the effect of the bankruptcy, civil rehabilitation or corporate reorganisation proceedings under Japanese law is extended to a debtor's assets outside Japan and an adjustment mechanism between the insolvency proceedings under Japanese law and one or more insolvency proceedings with respect to the same debtor under foreign law is provided for under these laws.

A foreign creditor will be treated in the same way as a Japanese creditor under the insolvency proceedings, including in relation to the exercise of any security interests it holds against a debtor.

Japanese courts will enforce a foreign judgment in Japan if:

- the foreign court is recognised as having jurisdiction over the case according to Japanese conflict-of-laws principles or relevant treaties;
- the defendant has been properly notified of the commencement of the proceedings or has not been properly notified but nevertheless assumed that proceedings had been commenced;
- the judgment or the procedure of the lawsuit is not against public policy in Japan (eg, punitive damages are against Japanese public policy); and
- there is reciprocity of recognition between Japan and the country where the judgment was issued.

For more than 70 years, Japanese law adopted the 'territoriality principle' whereby insolvency proceedings initiated in Japan do not extend to the debtor's assets outside Japan and insolvency proceedings initiated outside Japan will not extend to the debtor's assets in Japan. This policy has long been criticised by overseas as well as domestic practitioners and, in 2000, the insolvency laws were amended to resolve this issue (for details of these laws, see above). However, the UNCITRAL Model Law has not yet been adopted in Japan.

## COMI

### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

Under the ARAFIP, the concept of the 'debtor's principal business office' is essentially equivalent to the COMI under the UNCITRAL

Model Law. Although 'debtor's principal business office' is not defined under the ARAFIP, a recent court precedent held that, to decide the location of a 'debtor's principal business office', the Japanese court would take into account the various elements of the debtor as a whole, in particular the location of the debtor's headquarters or centre of business management and strategy, and the debtor's major asset and business operation. There is no explicit test or court precedent to determine the location of the 'principal business office' of a corporate group of companies, but a similar approach should be taken as summarised above.

## Cross-border cooperation

### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

The ARAFIP addresses the relationship between domestic and foreign proceedings in Japan. Under the ARAFIP, a foreign administrator may file a request to the Japanese court (ie, Tokyo District Court) to recognise the foreign proceedings and take necessary measures including the foreclosure of assets and appointment of a domestic administrator in Japan. After the ARAFIP has been effective in 2000, there are several precedents where foreign insolvency proceedings have been recognised in accordance with the ARAFIP.

The Bankruptcy Law, the Civil Rehabilitation Law and the Corporate Reorganisation Law also address the cooperation between domestic administrators and foreign administrators in cross-border insolvency and restructurings. For example, under these laws, domestic administrators may ask foreign administrators to provide any information needed. In addition, the laws provide a mechanism under which foreign administrators may file a petition in Japanese insolvency proceedings. Furthermore, the laws also allow foreign administrators to participate in domestic proceedings on behalf of creditors who participated in a foreign proceeding but not in a Japanese one. This will apply to domestic administrators in Japan on a reciprocal basis. To give a recent example, in its decision of 31 July 2012, the Tokyo District Court refused to recognise a foreign insolvency proceeding initiated by a debtor's insolvency administrator appointed in Italy. Under the ARAFIP, the court shall refuse to recognise a foreign insolvency proceeding in respect of a debtor if another foreign insolvency proceeding in respect of the same debtor has been already recognised in Japan and such recognised foreign insolvency proceeding constitutes the debtor's 'primary foreign proceeding'. Under the ARAFIP, 'primary foreign proceeding' for a business enterprise is defined as a foreign insolvency proceeding petitioned for in the country where the debtor's principal business office is located (see question 48 for more details of the meaning of 'principal business office'). In this case, the Tokyo District Court has already recognised a foreign insolvency proceeding



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in respect of the same debtor initiated in the US and it held that the US insolvency proceeding constitutes the debtor's 'primary foreign proceeding'. Therefore, in accordance with the ARAFIP, the debtor's foreign insolvency proceeding initiated in Italy has been refused recognition in Japan.

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**Cross-border insolvency protocols and joint court hearings**

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- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

Japan is not a signatory to any protocols or other arrangements to coordinate proceedings with courts in other countries. Also, there is no precedent of a Japanese court communicating with or holding joint hearings with courts in other countries.

# Luxembourg

Christel Dumont

Dentons Luxembourg

## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The following types of procedures are provided for under Luxembourg law: bankruptcy (under articles 437 ff of the Luxembourg Commercial Code (the Commercial Code)), controlled management, reprieve from payments and composition with creditors to avoid bankruptcy.

To determine if a debtor is bankrupt, two criteria are to be met cumulatively: the inability to pay due debts and the inability to raise credit.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The insolvency process is dealt with by the commercial courts and by the commercial chamber of the Court of Appeal. There are restrictions on the matters that the court may deal with in case of dispute of a creditor's claim. If the insolvency administrator disputes the claim of a creditor, such dispute may not be considered a commercial matter (if the creditor is an employee, for example). In such a case, the dispute will be dealt with by the court having jurisdiction (Civil Court or Labour Court, for example).

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Individuals and corporate entities exercising civil activities are excluded from bankruptcy procedure. Apart from the two cumulative conditions (inability to pay due debts and inability to raise credit), to apply for bankruptcy, it is necessary to be a commercial entity or an individual exercising commercial activities.

Moreover, the financial sector deals with its own regulations (the Law of 5 April 1993 on the financial sector, the Law of 30 March 1988 on undertaking for collective investment, and the Law of 6 December 1991 on the insurance and reinsurance sector).

A certain number of assets are protected from insolvency proceedings involving a physical person (clothes, personal goods, some furniture).

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

To date, Luxembourg has never had any insolvent public enterprises. No specific law or proceedings exist for this type of company.

## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

On 12 December 2012, the CSSF (Luxembourg financial regulator) published Circular 12/552 on central administration, internal governance and risk management, which was a first step towards transparency and more control by the CSSF according to EBA recommendations.

Moreover, on 1 April 2015 a law constituting the committee on systemic risk became effective, which implements two recommendations of the European committee on systemic risk (recommendation CERS/2011/3 and CERS/2013/1). The Committee is tasked with monitoring and preventing the development of systemic threats to the stability of the Luxembourg financial sector. Since the adoption of the law on 1 April 2015, the CSSF has issued several regulations further to advice published by the Committee:

- CSSF Regulation No. 15-04 on setting a countercyclical buffer rate dated 30 November 2015;
- CSSF Regulation No. 15-05 on the exemption of investment firms qualifying as small and medium-sized enterprises from the requirements to maintain a countercyclical capital buffer and a capital conservation buffer dated 30 November 2015;
- CSSF Regulation No. 15-06 concerning systematically important institutions authorised in Luxembourg, dated 30 November 2015;
- CSSF Regulation No. 16-01 on the automatic recognition of countercyclical capital buffer rates during the transitional period, dated 29 March 2016;
- CSSF Regulation No. 16-02 on setting the countercyclical buffer rate for the second quarter of 2016, dated 29 March 2016; and
- CSSF Regulation No. 16-03 on setting the countercyclical buffer rate for the third quarter of 2016, dated 28 June 2016.

## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

Three types of security could be used for immovable property:

- mortgage, which allows the mortgagee to sell the property upon default of the debtor through a public auction and to use the proceeds of the sale to be reimbursed as a priority;
- mortgage's mandate, which allows creditors to register the mortgage at a later stage but without guarantees on its rank as mortgagee;
- vendor's privilege, which is automatically registered by the Mortgage Registration Office in case the property's price of sale is not entirely paid by the purchaser. It is equivalent to a mortgage; and
- *antichrèse* (antichresis) is the allocation of an immovable as security for an obligation; it involves dispossession of whoever establishes it. This type of security is rarely used.

## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

The most common security in Luxembourg for moveable property is the pledge, which is subject to the Financial Collateral Law (dated 5 August 2005 as amended). This law allows for a security arrangement

to be taken at any time during the entire period preceding the opening of a bankruptcy proceeding without any risk of clawback (during the suspect period); thereafter the appropriation of assets or their sale by the pledgee is allowed without any court authorisation and is a fairly quick procedure.

For tradesmen, the use of retention of title is also very common. The property of the asset is kept with the seller until full payment and it is opposable to the insolvency administrator under certain conditions.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Unsecured creditors may start legal proceedings to obtain a judgment (or an attachment) before the opening of a bankruptcy or controlled management. Depending on the type of proceedings (judgment or attachment), these processes can be time-consuming. After the opening of the bankruptcy proceedings, all rights of unsecured creditors are suspended. The pending attachment proceedings are stopped.

No special procedures apply to foreign creditors. Once bankruptcy proceedings are opened, unsecured creditors are prevented from starting legal proceedings and shall lodge their claim with the insolvency administrator.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

According to Luxembourg law on commercial companies, the shareholders may decide to wind up the company and open the liquidation process by a qualified majority (at least half of the share capital present or represented and at least two-thirds of votes) if the company is solvent. The liquidator appointed by the shareholders' meeting dissolving and liquidating the company replaces the management and carries on all necessary activities for the effective liquidation of the company. The company only continues to exist for the purpose of its liquidation.

Since the adoption of the law of 10 August 2016 amending the law on commercial companies of 10 August 2015, as amended and certain provisions of the Luxembourg Civil Code, a company owned by a sole shareholder can use the simplified dissolution procedure. As a result of such simplified dissolution, all rights and obligations of the dissolved company are automatically transferred to the sole shareholder without going through any liquidation stage. The decision to dissolve is taken by the sole shareholder at a shareholders' general meeting. Creditors are entitled, in the course of 30 days following the publication of the information on the dissolution in the Luxembourg trade and company register (RCSL), to request a Luxembourg court to order the sole shareholder to grant securities over the sole shareholder's assets, in favour of their receivables.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Bankruptcy can be declared by the Commercial Court at the request of any creditor. The creditor must summon the debtor before the court to request its bankruptcy and must attest that the two cumulative conditions of bankruptcy are fulfilled (inability to raise credit and inability to pay due debts). The bankruptcy entails the deprivation by the debtor of the administration of its own assets and leads the court to appoint an insolvency administrator. The assets of the debtor shall be managed by the insolvency administrator and divided between the creditors, taking into consideration their respective privileges and rank of priority.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Controlled management may be opened when a company has lost its creditworthiness or has difficulties in meeting all of its commitments, and its purpose is to help the debtor reorganise its business. Only the debtor may file a petition with the Commercial Court, which will either

reject or validate the procedure. Commissioners, appointed by the court, will control the management of the company and prepare a reorganisation plan. This plan must be approved by the creditors and the court to become compulsory.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

In Luxembourg, the sole initiator of a reorganisation procedure is the entrepreneur, the company itself. It means a creditor is not allowed to request the court to place the debtor in an involuntary reorganisation.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

The board of directors of a Luxembourg company is under a legal obligation to file for bankruptcy within one month as from the moment the two cumulative conditions are met. If the board of directors fails to file for insolvency within the requested time limit, they can be subject to both criminal and civil liabilities if the court estimates that in not complying with their obligation they have contributed to the bankruptcy.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

In controlled management proceedings, the court's decision to delegate a judge to assess the situation of the debtor until a final decision on the motion has been taken suspends subsequent implementing acts. Moreover, from the date of the decision, the representative body of the debtor cannot, under penalty of nullity, alienate, pledge or mortgage, or commit or receive a moveable asset without the written permission of the delegated judge. In practice, the directors assume the daily management, but for any exceptional transaction, they must request the approval of the delegated judge.

There is no specific provision for suppliers providing goods or services after the first judgment. Nevertheless, they are creditors of the 'mass', superseding the previous creditors. Creditors have no right of supervision and cannot interfere in the affairs of the company. Directors and officers are no longer free to manage the business as they deem fit; first, they are subject to the control or the authorisation of the delegated judge and, second, to the one of the commissioners.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

For controlled management proceedings, the court's decision to delegate a judge entails ipso jure and until a final decision on the motion has been taken the suspension of all subsequent implementing acts (ie, the enforceability of judgments is no longer possible). This also applies to secured creditors, with the exception of security holders benefiting from Financial Collateral Law provisions. The same applies to reprieve from payment as soon as it is pronounced.

With regards to bankruptcy proceedings, the bankruptcy judgment stops the exercise of civil proceedings against the person of the debtor, as well as any seizure at the request of the unsecured and non-privileged creditors, on the moveable and immoveable assets. However, secured creditors under Financial Collateral Law provisions are not concerned by this freeze of enforceability.

**Post-filing credit****16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

In the case of controlled management, during the first period (judge appointed to assess the position of the company), the debtor who needs financing could find an agreement and have it approved by the delegated judge. In such a case the creditor will be a creditor of the 'mass debt' born after the first judgment and will rank before unsecured creditors whose claim existed beforehand.

Luxembourg Financial Collateral Law does not allow a creditor to take security after the beginning of the procedure (bankruptcy judgment or, in controlled management, the first judgment appointing a delegated judge), except on the day of the judgment opening such procedure (and if the collateral taker can prove that he was not aware of the commencement of such procedure in case the security was taken after its commencement).

**Set-off and netting****17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

According to the Financial Collateral Law, close-out netting provisions are valid and enforceable against third parties and liquidators and are effective notwithstanding the commencement or continuation of reorganisation measures or liquidation proceedings, without regard for the moment when these provisions, including those providing for netting, were agreed upon or enforced (nevertheless only if created before the opening of any reorganisations or insolvency measures).

Without any contractual provisions, the legal set-offs foreseen by article 1289 ff of the Civil Code are possible and according to case law both in the case of controlled management and bankruptcy upon certain conditions (ie, set-off takes place only between two debts that have likewise as their object a sum of money or a certain quantity of fungibles of the same kind, and that are likewise liquid and due).

**Sale of assets****18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

Luxembourg laws are quite basic. Nevertheless, the practice has shown that the administrators and the courts are able to find pragmatic solutions.

The bankruptcy provisions are laconic: 'the insolvency administrator will organise the sale of real estate property, goods and moveable property'. Therefore the insolvency administrator will either sell property via an auction process or a free-handed sale. Luxembourg does not recognise pre-packaged sales, therefore the freehand sale or the auction are proposed by the insolvency administrator and approved by the court or by the juge-commissaire (judge-commissioner) for perishable goods; the administrator may sell asset by asset or an entire portfolio. The assets are usually acquired 'free and clear'. The administrator could propose innovative solutions like the sale of a real estate portfolio with the credit attached to the investment, but this will be done through multiparty agreement and the approval of the court.

As the administrator could engage his or her own liability in the sale process 'stalking horse' bids, even though not expressly forbidden, are not used. Credit biddings in sales are not foreseen as such but may be allowed through legal compensation and could happen if the offer of the creditor is the fairest one at market conditions.

**Intellectual property assets in insolvencies****19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

In Luxembourg, there is no text governing the fate reserved to IP assets in insolvencies and, consequently, general contract law must apply. Upon the opening of insolvency proceedings, an IP licensor or owner may terminate an agreement concluded with a bankrupt company only if it contains a specific provision authorising one of the parties to terminate the agreement, if the other is declared insolvent. The insolvency administrator may elect to terminate the agreement but shall respect its terms in order to do so, as there is no automatic termination. In the case of termination, the administrator will not be allowed to continue to use the IP rights.

**Personal data in insolvencies****20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

As there are no specific provisions on the use of personal information or customer data collected by an insolvent company, general law provisions on the protection of personal data would apply. The insolvent company shall have complied with legal requirements (declaration or authorisation depending on the type of processing of personal data it performed). The insolvency administrator shall also comply with such legal requirements, if processing personal data and if such processing is subject to an authorisation or a declaration.

**Rejection and disclaimer of contracts in reorganisations****21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

In controlled management, the debtor is not allowed to reject or disclaim an unfavourable contract. Moreover, only the commissioners have the right to do so after their appointment, if the contract was concluded during the suspect period and if the conditions of having such contract declared void are fulfilled (see question 39).

If the contract is simply unfavourable but not voidable, the principle is that all ongoing contracts continue unless the debtor, with the agreement of the delegated judge or the commissioners, decides to terminate it. This termination should comply with the terms and conditions of the contract.

The breach of contract by a debtor may allow the counterpart to claim for damages and in case of success the payment of damages will be privileged at the same rank as the other claims arising after the opening of the reorganisation proceeding.

**Arbitration processes in insolvency cases****22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

The acceptance of claims in the bankruptcy estate cannot be arbitrated, but arbitration might be used to solve disputes regarding agreements signed by the bankrupt company before bankruptcy, in which an arbitration clause was inserted. New arbitration proceedings would involve the insolvency administrator and, pending arbitration, proceedings at the time of opening of the insolvency proceedings would normally continue after the insolvency case is opened. If the party to an arbitration

proceeding launched prior to the insolvency has lodged its claim with the insolvency administrator, the arbitration proceeding is stayed until the claim is accepted by the insolvency administrator.

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### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

Commissioners, appointed by the court, shall prepare a plan for the reorganisation of the business of the company. The reorganisation project equitably takes into account all interests at stake, such as the rank of the secured creditors. It must be accepted by a majority of more than 50 per cent of the creditors representing more than half of the liabilities. Then, it shall be ratified by the court. The release in favour of non-debtor parties is not foreseen in the provisions governing reorganisation.

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### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

In Luxembourg there is no procedure for expedited reorganisations. Bill of Law 6539, to be adopted at the end of 2016 or early 2017, foresees an 'administrative liquidation' and not a reorganisation of entities without any activity.

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### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

If the reorganisation plan is not approved, either by creditors or by the court, the latter may open the bankruptcy procedure if the conditions for bankruptcy are met. If the debtor fails to perform the plan, the court can also open a bankruptcy procedure upon request of the creditors or on its own motion.

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### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The first notice is given by the publication in relevant newspapers of an extract of the bankruptcy judgment indicating the time frame for the creditors' declaration of claims, for the closure of the official report on the admissibility of claims and for the hearing on the disputes arising from the discussion on claim admissibility. The insolvency administrator shall also send a notice to all known creditors to inform them of the time frame to lodge their claim.

The insolvency administrator has reporting obligations only to the supervising judge and to the public prosecutor but no specific obligation towards creditors.

Eventually, when the bankruptcy is completed, the creditors will be convened by the insolvency administrator to discuss the insolvency administrator's liquidation accounts.

The insolvency administrator has no other obligations to inform the creditors. If the case involves many creditors or if the amounts due are huge, the insolvency administrator on his or her own initiative can set up a dedicated website (or publicise in international newspapers) or keep the creditors informed by convening creditors' meetings once a year.

It is extremely rare that an insolvency procedure ends with a reorganisation plan (concordat). Either the liquidation is closed for shortfall of assets or the liquidation is closed without any further liability but again, in most cases, the unsecured creditors are not fully discharged.

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### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Only the insolvency administrator may pursue the estate's remedies. In such case the administrator's fees and expenses are paid by the state. The administrator could also have a contractual arrangement (approved by the judge supervising the bankruptcy) with creditors to have certain expenses paid by them, but in any case the final decision to sue somebody or to start proceedings to void certain transactions solely belongs to the administrator, and the assets obtained through the claim will be for the general benefit of all creditors.

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### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

A law dated 30 June 1930 provides that the judge commissioner designates an unsecured creditors' committee whose mission is to safeguard the interests of creditors in bankruptcy and composition to avoid bankruptcy.

The judge commissioner shall appoint a creditors' committee composed of three members from among the largest unsecured creditors, domiciled in the Grand Duchy or with a head office in this country. They receive no remuneration or compensation for their mandate. The mission of the creditors' committee is to assist the insolvency administrator and supervise the operations of the bankruptcy.

The creditors' committee is purely advisory. The possibility to retain advisers is not foreseen by the 1930 law. In practice, however, the possibility to form committees is hardly ever used.

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### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Luxembourg law does not contemplate the insolvency of a corporate group as a whole. Nevertheless, case law shows that for a group of companies with cross-collateralised debts, bankruptcy is generally pronounced on the same day for each Luxembourg company with the appointment of the same insolvency administrator. There is no specific provision in the law, but the administrator will have a general overview and may sell all the assets through an auction (for a real estate property portfolio, for example) or may find a more pragmatic solution by talking with the major secured lenders. No pooling is authorised except in specific cases.

In the case of opening of secondary proceedings in Luxembourg according to provisions or EU Insolvency Regulation 1346/2000, the liquidation surplus could be transferred to another EU country.

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### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

There is an automatic right of appeal in insolvency proceedings for any person who was a party in the first instance case without any requirement of obtaining permission to appeal. Some specific orders cannot be appealed, for example, orders appointing a new judge commissioner or a new insolvency administrator and orders authorising the sale of assets belonging to the estate. Foreign appellants (or applicants in first instance) may be required to provide security to pay the costs and damages to which they may be condemned (*cautio judicatum solvi*). The amount of security is determined by the court at its own discretion.

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**Claims**

- 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

The opening judgment, duly published, fixes a time limit to submit the declaration of claim (within a maximum of 20 days but this deadline is not compulsory in practice). The declaration should contain evidence of the claim. The same judgment fixes the court hearing for the verification of claims. In major cases like *Espirito Santo*, this hearing is postponed to give sufficient time to each creditor to lodge a claim. This hearing is conducted by the insolvency administrator in the presence of the judge commissioner and the debtor with the books of the debtor. A further court hearing allows the creditors to dispute the non or partial admissibility of their claim. The creditor whose claim has been rejected may appeal the court decision.

With regards to assignment of claim, the rules of article 1690 of the Civil Code apply (ie, the insolvency administrator shall be notified by the assignee).

Claim for contingent or unliquidated amounts could be accepted for a provisional amount provided they are certain.

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**Modifying creditors' rights**

- 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

In a bankruptcy proceeding, there is no legal provision allowing the court or the insolvency administrator to change the rank of a creditor. As the rank of creditors is established by the law, it is intangible. Nevertheless, the insolvency administrator could challenge the security taken by a creditor in the context of voidable transactions (see question 39).

The same rule applies to controlled management and the law foresees expressly that the reorganisation plan should respect the rank of priority of secured creditors.

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**Priority claims**

- 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Once the fees and expenses of the bankruptcy estate have been reimbursed, and once the employee-related claims (super-privileged salaries, ie, the last six months' wages amounting to a maximum of six times the minimum social salary or indemnification resulting from the termination of the employment agreement) have been paid, the rank of priorities is as follows:

- employees' contribution to social security;
- taxes (direct and indirect);
- employers' contribution to social security;
- landlord, pledgor not under the Financial Collateral Law and vendor's privilege; and
- unsecured debts.

No creditor has priority over secured creditors having security over assets through a pledge agreement (under the Financial Collateral Law) or having a mortgage.

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**Employment-related liabilities in restructurings**

- 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

Pursuant to article L.125-1 of the Luxembourg Labour Code the employment contract is terminated with immediate effect if the employer is declared bankrupt. However, according to case law, the insolvency administrator shall follow the normal process of termination of employment agreement, and specific provisions of collective redundancy where applicable. Article L.126-1 states that the Employment Fund

must guarantee wage claims and compensations arising from employment contracts, which are due to employees at the date of the judgment declaring the bankruptcy and outstanding for the last six months of work, and those resulting from the termination of the employment contract. Moreover, according to article 545 of the Commercial Code, these claims and indemnities will be listed as privileged claims at the same rank and in the same conditions as the privilege established in article 2101 of the Civil Code.

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**Pension claims**

- 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

The complementary pension regime is ruled by the law dated 8 June 1999 as amended. It could be put in place through a pension fund or a group insurance. This law states that insurance must cover the insolvency risk and includes the controlled management regime and not only the bankruptcy. The employees are fully covered except for raises granted by the employer during the two previous years.

There is no specific provision with regards to unpaid contributions by the employers (ie, no indemnification of the pension fund or group insurance for the non-payment of contributions).

The contribution to the legal regime of social security is privileged (see question 33).

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**Environmental problems and liabilities**

- 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

A company or an entity exposed to environmental matters should obtain during its corporate life cycle an administrative authorisation (commodo incommodo) to comply with environmental legislation. At the opening of an insolvency proceeding, the insolvency administrator shall prepare a declaration of termination of activity to the environmental administration. The Luxembourg courts have ruled that it is the insolvency administrator who is liable for this declaration. This declaration could foresee a clean-up and decontamination plan to be followed by the administrator. The amounts involved will be debts born after the opening of the bankruptcy (privileged but *pari passu* with similar debts). In practice, with mortgages on the property, the administrator would not be able to pay the cost of cleaning up.

Luxembourg legislation and case law apply the principle of 'polluter pays'. Moreover, if a fault of directors in the application of the environmental law can be proven, the administrator may also sue them. The creditors are not concerned by this liability.

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**Liabilities that survive insolvency proceedings**

- 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

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**Bankruptcy**

After the closure of the bankruptcy operations for insufficient assets, the creditors may undertake their individual actions against the bankrupt entity and the bankrupt property. However, if the bankrupt debtor has not also been declared wrongfully bankrupt or fraudulently bankrupt (see question 41 for criminal provisions) it cannot be sued by its creditors, unless it returns to better fortune within seven years of the closure of bankruptcy for insufficient assets or of having been convicted of simple or fraudulent bankruptcy.

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**Controlled management**

The judgment approving the proposed reorganisation plan is compulsory for all creditors who cannot sue the debtor for any outstanding balance.

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**Distributions**


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**38 How and when are distributions made to creditors in liquidations and reorganisations?**
**Bankruptcy**

The remaining amount of the bankrupt's assets, beyond the payment of fees and expenses of the administration of the bankruptcy, other claims born after the opening of the bankruptcy and the sums paid to secured creditors according to their rank, will be distributed among all admitted creditors *pari passu*. The insolvency administrator is allowed to pay interim dividends at his or her own responsibility, taking into account the existence of secured creditors, the rank of creditors and provisions for claims not yet admitted but declared.

**Controlled management**

The reorganisation plan establishes the percentage of distribution by taking into account the rank of creditors, the fees of the commissioners and those of experts appointed by the court. Such fees are considered as disbursements, charged to the debtor and are paid by privilege.

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**Transactions that may be annulled**


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**39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

The following transactions undertaken during the suspect period (set by the court, see question 40) and up to 10 days must be declared null and void (it is not automatic and the insolvency administrator is obliged to launch court action):

- disposition of assets without consideration of material adequacy;
- payments of debts, which had not fallen due, whether the payment was in cash or by way of assignment, sale, set-off, or by any other means;
- payments of debts, which had fallen due, by any means other than in cash or by bills of exchange; and
- mortgages or pledges granted to secure pre-existing debts.

Any other transactions made during the suspect period may be declared null and void if the insolvency administrator is able to prove that the counterpart knew of the cessation of payments. All acts or payments made to defraud the creditors will be declared null and void, regardless of the date on which they were made.

In controlled management, the debtor cannot, under penalty of nullity, alienate, pledge or mortgage, commit or receive a moveable asset without the written permission of the delegated judge, during a period starting at the date of the court decision appointing a judge in order to assess the situation of the debtor and ending on the date a final decision on the request of the debtor has been taken.

At a later stage, if the court decides to grant the controlled management and to appoint commissioners, such commissioners may launch court action, likewise an insolvency administrator, as described in the first paragraph above, upon prior court approval. They may also start legal action without court approval in the case of fraud.

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**Proceedings to annul transactions**


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**40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

At the issuance of the bankruptcy judgment, the court determines a 'suspect period', starting from the date of the suspension of payment, but not exceeding six months. The insolvency administrator solely has the power to act in order to void certain transactions (see question 39). In controlled management, the court may also determine a 'suspect period', if the court ascertains that the company being placed under controlled management has ceased its payments and the commissioners appointed can launch legal proceedings (see question 39).

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**Directors and officers**


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**41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

In general, prudent and diligent directors are not liable for their corporation's obligations. Nevertheless the general tax act mentions in its articles 108 and 109 a responsibility of corporate officers and directors in case of non-payment of taxes and personal fault with a possibility to ask them for payment instead of the company. According to case law, the simple fact of not having paid the taxes during the corporate lifecycle of the company constitutes a fault.

Moreover, directors of companies are liable for the increase of a company's debts if they did not file a petition for bankruptcy within one month of having met the bankruptcy conditions (see question 13).

Eventually, the directors (*ipso jure* or *de facto*) can be subject to the extension of bankruptcy, the action to bridge insufficiency of assets (misappropriation of assets) and, on a criminal side, to wrongful or fraudulent bankruptcy.

Directors may also be held liable for pre-bankruptcy actions under general corporate law provisions or under civil law or criminal law provisions.

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**Groups of companies**


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**42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

Neither Luxembourg law nor EU Insolvency Regulation 1346/2000 have provisions regarding the insolvency of a group. The principle is that any shareholder of a limited company (SA and SARL) is sheltered by a limited liability. Nevertheless, in the event of a bankruptcy, a shareholder of a limited company might be liable for the liabilities of related parties. This is called *comblement de passif* ('coverage of liabilities' of the debtor) by the *de facto* directors (any entity interfering in the company's operational business, disregarding the competence of the competent management body).

The theory of piercing the corporate veil could also be used to hold a parent company responsible for affiliates' liabilities, for example in the case of misappropriation of assets. But these cases are quite rare.

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**Insider claims**


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**43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

Luxembourg has no specific provisions regarding the right to claim of insiders. Shareholders' loans for instance are not disqualified in equity.

Nevertheless, non-arm's length creditors could fall in the scope of clawback actions and their claim could be declared null and void.

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**Creditors' enforcement**


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**44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

The Financial Collateral Law ensures that national and foreign insolvency procedures and reorganisation measures do not affect the enforceability of the pledge. As a result, it is forbidden for the commissioner, liquidator and receiver to set the collateral aside; and the secured creditor is allowed to enforce its pledge (or any collateral) without having obtained any consent of the insolvency administrator or the court even without giving prior notice.

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**Corporate procedures**


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**45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

The formal liquidation of a Luxembourg commercial company is governed by the law on commercial companies of 10 August 1915 as amended (see question 9). This procedure requires a general shareholders' meeting to decide to wind up the company and put it into liquidation. Following the decision to dissolve the company, one or

### Update and trends

On 1 February 2013, the Luxembourg government filed a new bill of law (Bill No. 6539 (the Bill)) on the protection of undertakings and the modernisation of insolvency law. The Bill intends in particular to modernise the Commercial Code and to set new rules in order to identify financially distressed undertakings more efficiently.

The Bill has four main components:

- a preventive component, inspired by Belgian law, which includes conservative measures to prevent distressed entities from being automatically declared bankrupt;
- a restorative component, which grants a second chance to unlucky traders, on the condition that they have acted in good faith and have not been held as the debtor of the remaining debts of the company after the closure of insolvency proceedings;

- a repressive component, which aims to prevent traders acting in bad faith by neglecting a business in order to start a new one, to simply escape with total impunity; and
- a social component, with a labour planning process aiming to maintain employment during reorganisation proceedings.

Furthermore, a new administrative winding-up procedure without opening bankruptcy proceedings will be introduced for empty shell companies.

The adoption of the Bill will significantly amend the insolvency and reorganisation regimes in Luxembourg.

several liquidators are appointed to manage the liquidation of the company. After the final general shareholders' meeting, the company shall be definitively liquidated and will be struck off the trade register. The duties of the liquidator are quite similar to the duties of an insolvency administrator (ie, realise the assets and pay the creditors on the assets, but in a corporate voluntary liquidation, all creditors shall be reimbursed).

As mentioned in question 9, simplified dissolution is also available for a Luxembourg company owned by a sole shareholder. In such simplified dissolution, there is no liquidation stage and no liquidator appointed as all rights and obligations of the dissolved company are automatically transferred to the sole shareholder.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

##### Bankruptcy

The assets of the bankrupt company shall be managed and sold by the administrator and divided between the creditors, taking into consideration their respective privileges and rank (see question 33), under supervision of the judge in charge of the bankruptcy (judge commissioner). Once all funds have been paid, an application is filed with the court for the termination of the bankruptcy proceeding, on the condition that all payments bound to be made were used. Then, the court declares the closing of the bankruptcy.

##### Controlled management

For the purpose of reorganisation, if and when the plan is approved by the court, it becomes compulsory for the business entity, all its creditors, co-debtors and guarantors. The sale of assets is fixed in the plan and different proportions are paid to creditors at different times, taking into consideration the nature, the size of their debts, pledges and mortgages or other guarantees. The court can also not interfere in the execution of the plan that has been approved. If the plan is unsuccessful, the court may terminate it and declare the company bankrupt. The court may also decide to reject the plan and dismiss the application for a controlled management procedure. In this case, it may open the bankruptcy procedure if the conditions for a bankruptcy are met.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

The UNCITRAL Model Law has not been adopted and it is not under consideration in the near future.

#### Recognition of foreign judgments within the scope of the EU

### Insolvency Regulation

An insolvency proceeding started in another member state will be automatically recognised in Luxembourg. Based on the provisions of EU Insolvency Regulation 1346/2000, foreign main insolvency proceedings opened in a member state of the European Union will be recognised immediately in other member states.

#### Recognition of foreign judgments outside the scope of the EU Insolvency Regulation

On the basis of the principles of 'universality' and 'unity' of the insolvency proceedings resulting from case law, foreign insolvency decisions are generally recognised (without any proceedings being required), if the following conditions are fulfilled:

- if they are lawfully made judgments (ie, rendered by a competent court – case law generally holds that insolvency proceedings can only be filed before the jurisdiction determined by the location of the debtor's centre of main interests – not obtained by way of fraud, due process has been complied with and not contrary to Luxembourg public policy); and
- if the judgment itself has international effect in the jurisdiction of origin (ie, if the law of the country where the judgment has been issued has extraterritorial scope. If not, the judgment will only have effect in this country).

The powers of the bankruptcy receiver are immediately recognised and he may collect assets locally. The debtor is no longer permitted to dispose of its assets located in Luxembourg and the enforcement rights of the creditors are suspended.

If the foreign bankruptcy receiver wishes to give effect to enforcement measures set out in the foreign judgment on assets located in Luxembourg, an enforcement order (exequatur) is required.

There is no condition of reciprocity.

Foreign creditors and local creditors are treated equally in insolvency proceedings opened in Luxembourg. Non-EU creditors must specify an address for service in Luxembourg.

### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

Luxembourg decisions are largely inspired by Eurofood (C-341/04 of 2 May 2006). The Luxembourg Court of First Instance (TA Lux, 9 February 2007, No. 105710) held that 'in order to locate the centre of main interests, one needs to establish a body of concordant indicia, such as the place of the board of directors meetings, the law governing the main contracts, the location of the business relations with the customers, the place where the commercial policy is defined, the location of the creditor banks and the centralised management of the purchasing policy, the staff, the accounting and the technology system'. In another decision, the Court of Appeal held that the COMI of the company was located in France (CA Lux, 12 November 2008). In this decision, the court focused on the location of the company's infrastructure and on the elements showing the place where the company exercised its business activity and managed its customer and supplier

relationships. The Court of Appeal gave less importance to elements such as the place where the board of directors met or the place where the company received mail or the fact that some suppliers still invoiced the company at its registered office.

There is no case law regarding the COMI of corporate group of companies.

#### Cross-border cooperation

**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

Luxembourg courts, even if there are only a few cases, generally have no problem in recognising the opening of a main proceeding in another member state (CA Lux, 2 December 2009, No. 34882 and TA Lux No. 447/08, 28 March 2008). Recognising a foreign insolvency proceeding is, likewise, not an issue in general.

Luxembourg faced major international insolvency cases during the past decade (Icelandic banks, Lehman Brothers, Madoff) mainly in the financial sector, but also in 2014 with Espirito Santo Luxembourg holding companies. The courts have always cooperated with other countries. The fact that Luxembourg judges generally speak French, German and English obviously makes cross-border communication

easier. In the Madoff cases the liquidators were obviously in touch with their US counterparts, and it was the same for Lehman Brothers. Regarding Landsbanki, there were some difficulties for the public prosecutor and the insolvency administrator to accept the fact that criminal investigations should be made; it was not exactly a refusal to cooperate but a different perception of the facts.

#### Cross-border insolvency protocols and joint court hearings

**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

The most recent and relevant case is *Lehman Brothers*, where a cross-border insolvency protocol for the Lehman Brothers Group of Companies was established by various entities of the group (world-wide) and the Luxembourg judiciary liquidators requested the court to modify the liquidation judgment in order to allow them to adhere to this protocol. The court agreed for the provisions that did not conflict with Luxembourg public policy. In any case, Luxembourg courts have already agreed to protocols in the 1990s when the various entities of BCCI group signed a pooling agreement despite the opening of insolvency proceedings.

No joint court hearings were initiated by Luxembourg courts.

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# Malaysia

Lee Shih and Nathalie Ker

Skrine

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

Insolvencies and reorganisations in Malaysia are governed by the Companies Act 1965 (the Act) and its related subsidiary legislation.

For a compulsory winding up that is a winding up through the court process, there are various grounds to wind up a company on the ground of insolvency. The most common ground is the inability of the company to pay its debts (section 218(1)(e) of the Act). Under section 218(2) of the Act, a company is deemed unable to pay its debts if:

- it has failed to comply with a statutory demand (being a demand served on a company by a creditor requiring payment of a debt within 21 days of service of that demand);
- execution or other process issued on a judgment, decree or order or any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or
- it is proved to the satisfaction of the court that the company is unable to pay its debts; and in determining whether a company is unable to pay its debts the court shall take into account the contingent and prospective liabilities of the company.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Matters involving the liquidation or reorganisation of companies in Malaysia are dealt with by the High Court of Malaya. There are no restrictions or limitations on the jurisdiction of the High Court to deal with corporate insolvency matters.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Although all companies are subject to the insolvency provisions under the Act, there are provisions in industry-specific legislation imposed on the insolvency of certain entities. These include: electricity licensees (Electricity Supply Act 1990), banks (Financial Services Act 2013), licensed investment banks (Financial Services Act 2013), licensed insurers (Financial Services Act 2013), trust companies (Trust Companies Act 1949), the Stock Exchange (Capital Markets and Services Act 2007) and business trusts (Capital Markets and Services Act 2007).

If assets of the company are subject to security (for example, assets subject to a charge), these would be excluded from the winding up process unless the secured creditor surrenders the security.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There are no special procedures for the insolvency of a government-owned enterprise. Creditors of insolvent public enterprises would have

the same remedies as those of private companies (ie, winding-up proceedings, creditors' voluntary winding up and schemes of arrangement (see question 1)).

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

There is no legislation in Malaysia that applies specifically to the financial difficulties of institutions on the ground that they are 'too big to fail'. However, certain industry-specific legislation governs the winding up of entities with a 'public interest' element, such as electricity licensees and banks (see question 3).

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

The principal type of security taken on immovable property is a registered charge. Land ownership in Malaysia is governed by the National Land Code and is based on the Torrens system. Other forms of security taken by lenders on real property include a lien created under section 281 of the National Land Code by the deposit of title deeds with the lender.

Section 108 of the Act requires a charge to be lodged with the Companies Commission of Malaysia (CCM) within 30 days after the creation of the charge. If the charge is not registered, the charge will be void against the liquidator and any creditor of the company.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

The principal types of security taken on moveable property are fixed and floating charges. Liens, pledges, assignments and retentions of title are also other forms of security.

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## Unsecured credit

### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

The main remedies and enforcement actions available to unsecured creditors in respect of unpaid debts include:

- filing a suit in the appropriate court to obtain judgment for the unpaid debt: Following judgment, a creditor may seek to enforce the judgment in a number of ways. These include applying to a court for a warrant of seizure and sale, and issuing garnishee proceedings; and
- issuing a statutory demand against a company: Where the debt exceeds 500 ringgit, a statutory demand may be issued against the company, requiring the company to pay the debt within 21 days of service. There is no strict requirement to obtain judgment before issuing the statutory demand. If the company fails to respond to the statutory demand, it will be deemed to be insolvent. Winding-up proceedings can then be initiated against the company (see

question 1). The process of applying for a winding-up order until grant of the order may take between three and six months. Once the winding up order is issued, the process of liquidation may take another six months to two years, depending on the complexity of the matter.

Under section 19 of the Debtors Act 1957, a creditor may apply for the seizure of a judgment debtor's property before judgment if the creditor can show a good cause of action and that, among others, the debtor has removed or is about to remove its property with the intent to delay the execution of judgment.

Further, creditors may apply for freezing orders if there is a risk of the judgment debtor dissipating its assets before judgment.

There are no special procedures in relation to foreign creditors. However, where there is a foreign judgment, this has to be registered in the Malaysian court under the Reciprocal Enforcement of Judgments Act 1958 (REJA). Once the judgment has been registered, it is enforceable in Malaysia in the same manner as a local judgment. If the foreign judgment does not come within the REJA scheme, the foreign creditor would have to bring fresh proceedings in the Malaysian courts to sue on the foreign judgment as a debt.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

The debtor company can initiate two types of voluntary winding up. The first is the members' voluntary winding up and the second is the creditors' voluntary winding up.

In a members' voluntary winding up, the directors must first make a declaration of solvency and lodge this with the CCM. The members then pass the resolution for the winding up of the company.

In a creditors' voluntary winding up, the directors must make a declaration that states that the company cannot continue its business by reason of its liabilities. The members will pass the resolution for the winding up of the company and appoint a liquidator. A creditors' meeting is called where the creditors may also vote on their choice of liquidator. The creditors' choice of liquidator would override the members' choice.

The effects of the commencement of a voluntary winding up are as follows:

- the company will cease to carry on its business, except where the liquidator is of the opinion that this is required for the benefit of the winding up process;
- the corporate state and corporate powers of the company shall continue until the company is dissolved; and
- any transfer of shares (unless made with the permission of the liquidator) and any alteration in the status of the members made after the commencement of the winding up will be void.

Specifically in a creditors' voluntary winding up, there is a stay of legal proceedings against the company unless a leave of court is obtained.

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Creditors may apply for involuntary liquidation of a company (ie, winding up by the court, under section 217(b) of the Act). The creditor must establish that the company is unable to pay its debts. The most common method is the service of a written statutory demand, where if the company fails to pay the sum demanded within 21 days of the service of the demand, the creditor can then file the winding-up petition.

If the court grants the winding up order, the winding up is deemed to have commenced from the time of the presentation of the petition before the court.

The effects of the commencement of winding up by the court are as follows:

- any disposition of the property of the company, including shares, made after the commencement of the winding up proceedings will be void, unless the court orders otherwise;

- any attachment, sequestration, distress or execution put in force against the estate or effects of the company after the commencement of the winding up proceedings will be void; and
- all actions or proceedings against the company shall be stayed, and no actions may be commenced against the company, except by leave of the court.

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### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Formal financial reorganisation in Malaysia is carried out by way of a scheme of arrangement under section 176 of the Act. A scheme of arrangement is a court-approved compromise or arrangement between a company and its creditors (or any class of creditors).

One of the key objectives of a scheme of arrangement is to provide a mechanism to effect a formal compromise to bind dissenting creditors, so long as the statutory majority of votes has been achieved. The scheme will be subject to the approval of the court. It is common to have an external administrator, known as a scheme administrator, to assist in the scheme of arrangement procedure.

To initiate a scheme of arrangement, the company, a creditor or a member would have to apply to the court for an order for a meeting or meetings of the creditors or members to be held. The applicant has the flexibility in deciding which creditors or members to include in the proposed scheme of arrangement. When initiating a scheme of arrangement, the applicant can also seek a moratorium order known as a restraining order. The restraining order will restrain all further proceedings in any action or proceeding against the company, except by leave of the court.

At the meeting or meetings, the creditors or members will vote on the proposed compromise or arrangement. If a majority in number representing 75 per cent in value of the creditors or members agrees to the proposed compromise or arrangement, an application must be made to the court to obtain the approval of the court for the proposed compromise or arrangement. The court may grant its approval subject to such alterations or conditions as it thinks fit.

Once approved by the court, the compromise or arrangement is binding on all the creditors or members of the company expressly included in the scheme, and will be implemented according to its terms. Where the company is in the course of being wound up, the compromise or arrangement is binding on the liquidator and contributories of the company.

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### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

There are no provisions under the Act that enable creditors to commence an involuntary reorganisation.

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Under the Act, there are no provisions that compel companies to commence insolvency proceedings in particular circumstances. When a company is in winding-up proceedings, any officer of the company who is knowingly a party to a transaction, with no expectation that the company would be able to pay the resulting debt, can be subject to civil and criminal liability. The officer can be subject to criminal prosecution for insolvent trading. Upon conviction, the officer may be subject to civil proceedings where the court may declare the officer personally responsible for the repayment of the whole or any part of that debt.

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## Doing business in reorganisations

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- 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

### Scheme of arrangement

In a scheme of arrangement, the company's management continues to operate the business during the scheme of arrangement procedure.

Where there is no restraining order in place, the company can continue to incur debts and obligations, raise funding and sell its products and services in the ordinary course of business.

Where there is a restraining order in place, there are certain restrictions. Any disposition of the property of the company, other than those made in the ordinary course of business, shall be void unless the court otherwise orders. Where a company disposes of or acquires any property, other than in the ordinary course of business, without leave of the court, every officer of the company who is in default shall be guilty of an offence.

There is no special treatment given to creditors who supply goods or services after the commencement of the scheme of arrangement, provided that the goods and services are supplied in the ordinary course of business.

As for the roles of the creditors and the court, creditors are given no statutory role in the supervision of the debtor company's business activities. However, one of the requirements for the grant of a restraining order is that the court must approve a person nominated by a majority of the creditors to act as a director of the company.

### Winding up

Unlike the situation in a scheme of arrangement, the winding up order would then suspend the directors' and officers' powers of management over the company. However, the directors would still retain the residual power to appeal against the winding up order.

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## Stays of proceedings and moratoria

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- 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

### Scheme of arrangement

There is no automatic moratorium in a scheme of arrangement, and a restraining order would have to be obtained to stay legal proceedings against the company. See the answer to question 14 for more details.

### Winding up

In a compulsory winding up, there is no automatic stay of proceedings against the company after the presentation of the winding-up petition. However, at any time after a winding-up petition is presented, the company or any creditor or contributory may make an application to the court to stay further proceedings against the company.

Once a winding-up order is made or a provisional liquidator has been appointed, an automatic stay operates on proceedings against the company, unless the court grants leave for the continuation of the proceedings.

In a creditors' voluntary winding up, there is an automatic stay of proceedings against the company upon the commencement of winding up. This is unless the court allows the continuation of the proceedings and subject to such terms as imposed by the court.

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## Post-filing credit

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- 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

After the commencement of winding up (in winding-up proceedings by the court), certain transactions entered into by the company may be void if they amount to a disposition of the property of the company.

Thus, if the charging of property falls under a 'disposition of property', this may be void. However, the court may exercise its discretion to validate such a transaction, for example, if it can be shown that the transaction would be beneficial to the company and its creditors and if the court considers that the disposition is reasonable. Such loans or credit obtained would be subject to the same common law rules on priorities in liquidation.

Once the winding up order has been granted, the liquidator has the power to raise any money required on the security of the assets of the company.

For a company undergoing a scheme of arrangement, there is no prohibition in obtaining secured or unsecured loans or credit. If there is a restraining order in place, it may be prudent to then obtain leave of the court before obtaining such loans.

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## Set-off and netting

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- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

In winding up, creditors may set off credits, debts or other mutual dealings where these are mutual between the creditor and the debtor company. The creditor cannot exercise the right of set-off where he or she had notice of the winding up at the time of giving credit to the company.

In a scheme of arrangement, the right of set-off of a creditor would depend on the terms of the compromise or arrangement.

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## Sale of assets

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- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

In a scheme of arrangement and where there is no restraining order in place, the company may continue to sell its assets in the ordinary course of business. However, where a restraining order has been granted by the court, no disposition of property may be made out of the ordinary course of business, except with leave of the court. Under the Act, the court may also order the transfer of the whole or any part of the undertaking and of the property or liabilities of any company in the scheme to the designated transferor company. The purchaser of the assets will acquire the assets under the conditions specified in the scheme of arrangement.

In a winding up, any disposition of the company's property after the commencement of winding up is void unless ordered otherwise by the court. After the grant of the winding-up order and the appointment of the liquidator, the liquidator has the power to sell the assets of the company by private auction, public tender or private contract. Generally, the assets will pass free of liabilities, unless otherwise agreed between the liquidator and the purchaser.

Stalking horse bids and credit bidding are not common, but it is possible to carry out these procedures.

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## Intellectual property assets in insolvencies

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- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

There are no statutory provisions for the termination of a debtor's IP rights upon the commencement of winding up. However, parties commonly agree for such a termination in the agreement granting the licence. If there is no such clause, the debtor company may continue to benefit from the IP rights.

The liquidator in winding-up proceedings does not have the power to terminate an agreement for IP rights and to continue to use the rights

for the benefit of the estate, unless this is provided for in the agreement between the debtor and the licensor for the use of the IP rights. It is unlikely that such clauses would be present in a licence agreement.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The collection and use of personal data in Malaysia is governed by the Personal Data Protection Act 2010 (PDPA). Under the PDPA, companies incorporated in Malaysia must issue a written notice to the data subject setting out certain information, including the purposes for which the personal data is being processed and the class of third parties to whom the company discloses or may disclose the personal data. Quite commonly, such notices would inform the data subject that his or her personal information may be shared in the context of a winding up.

### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

The right of the debtor company in the midst of a scheme of arrangement to reject or disclaim an unfavourable contract would depend on the terms imposed by the compromise or arrangement.

If a debtor breaches a contract after winding up proceedings have commenced and is sued for the breach of contract, the debtor company may apply for a stay of the action. Where a winding up order has been granted, no proceedings may be brought against the debtor company unless leave of the court is obtained.

### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Matters that fall within insolvency proceedings are unlikely to be arbitrable in Malaysia. As for the continuation of arbitration proceedings, the court may grant a stay of such proceedings after the presentation of the winding-up petition, and an automatic stay operates after the grant of the winding up order. Leave from the winding-up court must then be obtained to continue such arbitration proceedings against the wound-up company.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

For a successful reorganisation by way of a scheme of arrangement, a majority in number representing 75 per cent in value of the creditors or class of creditors present and voting in person or by proxy must agree to the proposed scheme or compromise. In practice, separate meetings for the various classes of creditors (eg, secured, unsecured and preferential) have to be called where the rights of each class under the scheme differ widely, to enable each class to decide on the proposed scheme.

After the approval of the scheme of arrangement by the requisite number of creditors, the scheme will have to be approved by the court. Once the court grants an order approving the scheme of arrangement, the scheme will take effect upon the court order being registered with the CCM.

A proposed scheme of arrangement may release non-debtor parties from liability, subject to the approval of the creditors and the court.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

There are no procedures under the Act that provide for expedited reorganisations. However, the creditors and the company may pre-agree a reorganisation or restructuring to be effected by way of a scheme of arrangement. This may be carried out by the company entering into an agreement that binds creditors to vote in favour of the proposed scheme of arrangement.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A proposed scheme of arrangement cannot succeed if the requisite approvals from the creditors and the court are not obtained. If the debtor company fails to carry out an approved scheme, the creditors may institute proceedings to enforce their rights under the binding order granting approval for the scheme.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

This section will focus on the compulsory winding-up process. The directors and other officers listed in the Act shall submit within 14 days of the date of the winding up order a statement of affairs to the liquidator. This statement will essentially contain particulars of the assets, debts and liabilities of the company.

As soon as practicable after the receipt of this statement of affairs, the liquidator shall submit a preliminary report to the court on:

- the amount of capital issued, subscribed and paid up and the estimated amount of assets and liabilities;
- if the company has failed, the causes of failure; and
- whether in the liquidator's opinion, further inquiry is desirable as to any matter relating to the promotion, formation or failure of the company or the conduct of the company's business.

The liquidator may, from time to time, call for meetings of the creditors or contributories to ascertain their wishes in all matters relating to the winding up.

There may be circumstances where the court may direct that meetings of the creditors or contributories be held to ascertain their wishes.

The liquidator may, and shall, if requested by any creditor or contributory, summon separate meetings of the creditors and contributories for the purpose of determining whether or not the creditors or contributories require the appointment of a committee of inspection to act with the liquidator, and if so, who are to be members of the committee.

After a period of six months from the date of his or her appointment, the liquidator shall within one month, and for every subsequent period of six months, lodge with the CCM and the official receiver an account of his or her receipts and payments and a statement of the position in the winding up. The liquidator shall give notice that the account has been made up to every creditor and contributory when next forwarding any report, notice of meeting, notice of call or dividend. This notice shall inform creditors and contributories at what address and between what hours the account may be inspected.

In terms of the creditors pursuing the wound-up company's remedies against third parties, see question 27.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

It is possible for the creditors to directly or indirectly pursue the wound-up company's remedies. Firstly, creditors may agree to provide funding

to the liquidator for the costs of litigation. After assets have been recovered through such litigation, the court may make an order granting those creditors a priority in the distribution of assets in order to recover those costs of litigation. Therefore, the fruits of the litigation will be recovered for the general benefit of the unsecured creditors, but the creditors who provided the funding may obtain priority for the repayment of the funding.

Second, it is possible for the liquidator to obtain a court order approving the assignment of the proceeds from any litigation to repay the costs of the funding provided by creditors.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Following from question 26, in a compulsory winding up, the creditors and contributories can require the appointment, and decide on the composition, of a committee of inspection.

In administering the assets of the company, the liquidator must have regard to the directions given by the committee of inspection.

Further, the liquidator may only exercise the following powers with the approval of the committee of inspection (or of the court):

- carrying on the business of the company more than four weeks after the date of the winding up order;
- paying any class of creditors in full;
- making any compromise or arrangement with creditors;
- compromise any calls and liabilities and any claims in relation to the company; and
- appoint an advocate to assist the liquidator in his or her duties.

No member of a committee of inspection shall, except under and with the sanction of the court, directly or indirectly obtain any profit or payment for any services or for any goods supplied to the liquidator. The court sanction will only be given where the service performed is of a special nature.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Each company in the corporate group would be a separate legal entity, and the winding-up proceedings of each entity would be treated separately. Therefore, there would be no pooling together of assets and liabilities.

Regarding a foreign incorporated company that has a place of business or is carrying on business in Malaysia, where this foreign company is in liquidation outside of Malaysia, the assets recovered in Malaysia have to be first used to pay debts and settle liabilities incurred in Malaysia before paying the net amount to the liquidator of that foreign company.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

There is a right of appeal from court orders made in winding-up proceedings. In an appeal against the winding-up order, the directors maintain a residual right of management to have the company appeal against the winding-up order. Therefore, the consent of the liquidator is not required. There is no mandatory requirement to post security to proceed with an appeal, but it is common for the wound-up appellant to face an application for security for costs.

### Claims

#### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

A creditor will have to submit a proof of debt form. The liquidator will provide at least 21 days' notice for the date on which the creditors are to prove their debts or claims.

All debts payable on a contingency and all claims against the company, present or future, certain or contingent or sounding only in damages shall be admissible as proof against the company.

A creditor proving his or her debt shall deduct therefrom all trade discounts, but he or she shall not be compelled to deduct any discount, not exceeding 5 per cent on the net amount of his or her claim, which he or she may have agreed to allow for payment in cash. Interest can be claimed up to 6 per cent per annum from the time the debt or sum was payable until the time of payment.

For debts payable at a future time, a creditor may prove for this debt as if it were payable presently, but there will be a deduction of a rebate at a rate of 6 per cent per annum computed from the declaration of the dividend up until the time when the debt would have become payable.

The liquidator shall examine every proof of debt lodged with him or her and the grounds of the debt, and shall in writing admit or reject it, in whole or in part, or require further evidence in support of it. If he or she rejects a proof, he or she shall provide to the creditor the grounds of the rejection. Within 21 days of the service of the notice of rejection, the creditor can appeal to the court against this decision.

### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The court may not change the priority of a creditor's claim.

### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

##### Liquidation

Secured creditors can enforce their security, and they stand outside of the winding-up process. Where their security is inadequate, the secured creditor can submit a proof of debt for the balance.

The following claims have priority over unsecured debts:

- the costs and expenses of winding up, which includes the remuneration of the liquidator;
- subject to certain limits, all wages or salary (including commissions) of employees;
- all amounts due in respect of workers' compensation;
- all remuneration payable to an employee in respect of vacation leave;
- amounts due in respect of contributions to the employees' provident fund during the 12 months before the commencement of winding up; and
- all federal tax assessed before the commencement of winding up or assessed at any time before the date for proving debts has expired.

##### Scheme of arrangement

In a reorganisation through a scheme of arrangement, there is no priority of claims per se. The terms of the scheme as approved by the court would determine the manner in which the creditors will be paid.

### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

As set out in the answer to question 33, certain amounts due to employees enjoy priority in the distribution of assets in liquidation.

### Update and trends

The Companies Act 2016 has been recently gazetted in September 2016. It is likely to be brought into force in stages, starting in 2017. The new Act will revamp the existing provisions on winding up and schemes of arrangement. There will also be two new corporate rescue mechanisms: corporate voluntary arrangement and judicial management. Corporate voluntary arrangement is modelled after the UK provisions, while judicial management is similar to the Singapore provisions.

### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

As set out in the answer to question 33, amounts due in respect of contributions to the employees' provident fund during the 12 months before the commencement of winding up enjoy priority in the distribution of assets in liquidation.

### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

There are no specific statutory provisions dealing with insolvency proceedings and environmental issues. The environment-related laws will generally impose personal liability on any person who has committed an offence under the relevant statute. Therefore, personal liability could extend to the insolvency administrator, directors or officers of the company.

### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

In liquidation, no liabilities will survive the winding up and dissolution of the company. Similarly, in a scheme of arrangement, there will be no further liabilities once the company has discharged all its obligations under the terms of the scheme.

### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

This applies only in liquidations. The liquidator can declare interim dividends as and when the liquidator decides appropriate. Once the liquidator has completed the realisation of the assets, the liquidator can declare a final dividend.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The following types of transactions occurring prior to the commencement of winding up can be set aside:

- an undue preference, being a transaction between the company and a creditor where the creditor obtains a preference, priority or advantage over other creditors in the winding up;
- a transfer or conveyance of property to a third party that was either not made in good faith or without valuable consideration;
- sale at an undervalue or an acquisition at an overvalue of property, business or undertaking for a cash consideration where the counterparty is a director, or a company with the same director;
- with leave of the court or the committee of inspection, the liquidator may disclaim onerous contracts, such as any estate or interest in land that is burdened with onerous covenants, shares in corporations, and unprofitable contracts;

- a floating charge created within six months of the commencement of winding up. Such a charge shall, unless it is proved that the company was solvent immediately after the creation of the charge, be invalid except the amount of any cash paid to the company at the time or following the creation of, and in consideration of, the charge together with 5 per cent per annum interest; and
- after the commencement of winding up, any disposition or transfer of property of the company shall be void, unless otherwise ordered by the court.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

There is a time period during which transactions are potentially vulnerable to being set aside. The time period is calculated based on the date of commencement of winding up. For a compulsory winding up, it is from the date of the presentation of the winding-up petition. In a creditors' voluntary winding up, it is from the date on which the directors lodged the statutory declaration and appointed the provisional liquidator.

The time period depends on the nature of the transaction and can range from six months to five years.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Corporate officers and directors are generally not liable for their corporation's obligations. However, if these officers or directors are guilty of insolvent trading or fraudulent trading, the court may declare that they be made personally liable for the whole or part of the debts of the company.

Insolvent trading is where a director or other officer of the company, who was knowingly a party to the contracting of a debt, had no reasonable or probable ground of expectation (after considering the other liabilities of the company) of the company being able to pay that debt. The officer can be subject to criminal prosecution for insolvent trading.

Fraudulent trading is where any person, including a director or officer, is a party to the carrying on of the business of the company with the intent to defraud creditors of the company.

Further, when a company is insolvent or in a near-insolvent state, the directors' fiduciary duties extend to a duty to have regard to the interests of the company's creditors. The company (acting through its liquidator) may be able to sue a director for a breach of this duty.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

The parent and affiliated companies would all be separate legal entities and would generally not be responsible for the liabilities of the subsidiaries or affiliates. There may be the exceptional situation where the court allows for the piercing of the corporate veil such that the parent company may be held responsible for the liabilities of the subsidiary.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There are generally no restrictions on claims by such creditors unless these claims fall within one of the transactions liable to be set aside (see the transactions listed in the answer to question 39).

**Creditors' enforcement****44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

A debenture holder may have the power to appoint a receiver or receiver and manager over the charged assets. Even after the winding up of the company, the receiver or receiver and manager would have possessory powers over such charged assets.

**Corporate procedures****45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

There are corporate procedures for the winding up of a company. See the answer to question 9 where the members' voluntary and the creditors' voluntary winding-up process are set out.

A company may also be struck off the register, which would result in the company being dissolved. Where the registrar has reasonable cause to believe that a company is not carrying on business or is not in operation, he or she may send to the company a letter by post to that effect and stating that if an answer showing cause to the contrary is not received within one month from the date thereof a notice will be published in the Gazette with a view to striking the name of the company off the register.

**Conclusion of case****46 How are liquidation and reorganisation cases formally concluded?**

In a compulsory winding up, the process is concluded when the liquidator applies to the court for an order that he or she be released and that the company be dissolved when he or she has realised the property of the company and issued a final dividend.

A scheme of arrangement is concluded when all the obligations under the scheme have been discharged.

**International cases****47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Malaysia is not a signatory to any treaty on international insolvency or restructuring. The UNCITRAL Model Law on Cross-Border Insolvency has not been adopted in Malaysia.

Under the Reciprocal Enforcement of Judgments Act 1958, foreign judgments obtained from superior courts of certain jurisdictions are recognised once registered in Malaysia.

If a registered foreign company goes into liquidation or is dissolved in its place of incorporation, the foreign liquidator shall have the powers and functions of a liquidator in Malaysia until a liquidator in Malaysia is duly appointed by the court.

**COMI****48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

Malaysia does not recognise the concept of COMI.

**Cross-border cooperation****49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

See to the answer to question 47.

**Cross-border insolvency protocols and joint court hearings****50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

The courts in Malaysia do not have cross-border insolvency protocols or other arrangements with courts in other countries. There are no reported decisions where a Malaysian court has communicated or held joint hearings with courts in other countries in cross-border cases.

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# Mexico

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Oscós Abogados

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Commercial Insolvency Law (LCM) amended as of 11 January 2014, applies to merchants and traders, individual and legal entities, including commercial companies, trusts engaged in business activities, state-owned commercial companies, the estates of deceased merchants, partners of a liability partnership and small merchant debts lower than 400,000 unidades de inversión (UDIs, see question 11), subject to written agreement.

The insolvency of non-merchants (individuals, consumers) is governed by the state civil codes and state codes of civil procedure.

Insolvency for financial institutions, insurance, bonding, reinsurance and re-bonding companies is governed by their special laws.

Filing for insolvency is not mandatory.

The conditions for initiating general insolvency proceedings (concurso mercantil for merchants) are that there must be a debtor who is a merchant, individual or legal entity and there has been a failure to make payments generally when due.

Criteria for establishing a general default on payment obligations are:

- failure to meet payment obligations to at least two creditors;
  - obligations more than 30 days overdue;
  - such overdue obligations represent 35 per cent or more of the total amount of the debtor's obligations as of the petition filing date; and
  - the debtor must lack cash assets, as defined by the law, to pay at least 80 per cent of the total debts due as of the petition filing date.
- Cash assets are:
- cash on hand and deposits on site;
  - deposits and investments due within 90 days as of the date of the petition being filed;
  - accounts receivable due within 90 days as of the date of the petition being filed; and
  - securities that regularly registered sell-or-buy operations in relevant markets, saleable within 30 banking business days.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Federal district courts are the only courts with jurisdiction over commercial insolvency proceedings for merchants. Non-merchants are subject to state and local civil jurisdiction. The judiciary will set up specialised federal district courts dealing with insolvency matters.

Labour credits (see question 3) are included within the total liabilities of the debtor. However, labour creditors are not obliged to join the general insolvency proceedings (see question 9). Labour credits are, instead, considered under the jurisdiction of the labour courts and are enforced and paid before labour courts rather than joined to federal or state insolvency courts. The same applies to tax credits, which are considered under the jurisdiction of the tax courts.

It should be noted that the Federal Constitution (article 1) was amended on 10 June 2011, to recognise and guarantee human rights granted by the Constitution and international treaties. This amendment commands all authorities to recognise, promote, respect, protect

and guarantee human rights. Thus, pursuant to constitutional articles 1 and 133, all authorities, including the judiciary in all levels (first instance, appeal and constitutional) must enforce human rights through the operation of law, even without the party's petition and even if there is another conflicting provision. Human rights include, inter alia, not only life, liberty and freedom from discrimination, but also ownership, property, rights and obligations under contracts, due process, the effective administration of justice, effective judicial remedies, equal treatment and the enforcement of the rule of law.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Workers owed labour credits are excluded; such workers are governed by the Federal Labour Law (labour credits are claims by employees and may include unpaid wages and employment indemnity).

Tax claims and claims equivalent to tax claims by the tax authorities (federal, state and municipal), the Mexican Institute of Social Security (IMSS) and the National Workers' Housing Fund Institute (INFONAVIT) are excluded from the general bankruptcy proceedings (see question 9). 'Claims equivalent to taxes' includes the IMSS and INFONAVIT tax quotas employers and employees must pay that are considered equivalent to taxes. Federal tax credits are governed by the Federal Tax Code and state and municipal tax credits are governed by state tax laws. Labour creditors and tax creditors do not join the bankruptcy proceedings and are paid and liquidated by their labour chambers and tax authorities, respectively.

Tax credits and labour credits are included within the total liabilities of the debtor. Labour claims have super priority. Tax credits have priority over unsecured credits and over credits secured by a pledge or mortgage, provided these secured credits were perfected and recorded before the notice to debtor of the tax credits. Tax credits have no priority over labour credits or over alimony for which a lawsuit has been filed before a court.

By law, tax creditors do not join the general bankruptcy proceedings. The law provides that if a debtor is adjudicated in general insolvency proceedings, the court shall notify tax creditors of such adjudication. Enforcement of tax creditors may be stayed by this adjudication, provided tax creditors had been notified of the filing of the general insolvency proceedings petition.

There are assets excluded from execution, attachment and liquidation in bankruptcy such as alimony, child support, recorded homestead (family patrimony), tierras ejidales (communal real estate land) and life insurance in the case of an irrevocable appointment of a beneficiary.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The general bankruptcy proceedings govern the insolvency of a government-owned enterprise, when the government-owned enterprise is incorporated as commercial corporation or, when by virtue of law, the commercial law shall govern the government-owned enterprise,

as in the case of the newly productive enterprises Petroleos Mexicanos (PEMEX) and Comisión Federal de Electricidad (CFE). For remedies to creditors of insolvent public enterprises please refer to those discussed herein.

Consideration of the bill or act of incorporation and by-laws of a government-owned enterprise shall be taken into account for special regulations thereto and the applicability of a different insolvency regime, including, in some instances, the federal or state general insolvency proceedings.

Special public domain regulations on government-owned assets regime shall be considered as well, since they may not be subject to attachment, seizure or judicial auction sale. Creditors of insolvent public enterprises have as remedies the due process rights to claim, pursue and be paid based upon their priority, in accordance with the provisions governing the insolvency proceeding.

Consideration, shall also be given to public budget regulations for the payment of debts owed by a government-owned enterprise.

### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Under the new financial regime, the banking law provides for an autonomous, independent and special insolvency regime called 'judicial banking liquidation', in addition to the administrative control regulations. Such proceedings will be the federal district court-directed liquidation of a bank, and the trustee will be appointed by the Banking Commission. Accordingly, the amendments to the banking law, in the administrative regulation, give greater powers to the financial regulators and provide additional tools for the control, investigation, overview, preventive and protective measures, requirements, sanctions, etc, over banks and financial institutions, aimed at more efficiently preventing and remedying situations of financial distress.

On the other hand, amendments also provide legal tools for the efficient and prompt enforcement of financial regulators powers, liquidation of estate assets and creditors' collection rights. It is recognised that under the current LCM, the liquidation of a bank in bankruptcy may take up to a decade. Accordingly, in the new regime dilatory practices are overcome to make liquidation faster and more efficient.

### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

The principal types of security over immoveables are mortgages; industrial mortgages; aircraft mortgages; maritime mortgages; train mortgages; guarantee trusts; and purchase and sale contracts with retention of ownership title.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The principal types of security over moveables are: ordinary pledges; pledges with debtor's holding possession of pledges; guarantee trusts; bonding guarantees (surety bonds); insurance credits; and stock exchange securities liens. As collateral, the aval (joint and several personal guaranty on negotiable instruments, which is equivalent to a co-maker and is valid even though the direct obligation is null and void) personal guarantee on obligations and joint and several obligation is common.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Attachment on enforcement of final, res judicata judgment has priority in liquidation. Pre-judgment attachments, attachments and judgments regarding unsecured credit lack any priority in liquidation.

The processes are, in general, difficult and time-consuming. Allowed or disallowed claims may be appealed up to the Mexican Supreme Court, which might be costly and takes a long time.

Foreign creditors receive the same treatment as domestic creditors. Proofs of claim must be filed to enforce creditor's rights, to become a recognised creditor and to participate in reorganisation and liquidation.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Insolvency proceedings for merchants are a single, monolithic, compound process, namely general insolvency proceedings, comprising two major stages: conciliation and bankruptcy (liquidation). In conciliation a conciliator is appointed and seeks to establish a reorganisation plan. If no reorganisation plan is agreed, the process, by operation of law, is converted into bankruptcy (liquidation). A trustee is appointed for liquidation.

There is also a sub-stage: the visit, wherein a visitor is appointed to inspect the debtor's premises and accounts to confirm that the standard for insolvency is met and reports accordingly to the district court, which may judge the debtor to be in general insolvency proceedings.

Full insolvency proceedings may be voluntary or involuntary. In a voluntary petition or prepackaged insolvency there is no visit. In an involuntary petition a visit shall be conducted to confirm the insolvency standard is met. The debtor may voluntarily request general insolvency proceedings (merchant's insolvency) in the event of bankruptcy, for which there is no visit. Involuntary petition at the stage of bankruptcy is allowed if the debtor does not oppose it; otherwise, full insolvency proceedings shall be pursued. In involuntary bankruptcy a visit shall be conducted. Bankruptcy allows for a reorganisation plan. Bankruptcy relief becomes available when the debtor (merchant) requests his or her bankruptcy. Voluntary bankruptcy is adjudicated without full insolvency proceedings (see question 11) and in involuntary bankruptcy when the debtor does not oppose it. For a debtor to be placed in bankruptcy by a creditor (ie, involuntarily) full insolvency proceedings shall be pursued from the stage of conciliation unless the debtor agrees to its bankruptcy. A debtor is declared to be in bankruptcy by the court if a plan is not agreed upon during conciliation proceedings or if the debtor does not cooperate with the plan and the conciliator (see question 11) requests a declaration of bankruptcy.

In order to adjudicate a debtor in general insolvency proceedings, insolvency standard and law requirements shall be met, whether voluntary or involuntary and whether petition is to be opened as of the conciliation or bankruptcy stage. The general insolvency proceedings adjudication determines the respective stage. The effects of the respective stage are provided by this declaration and by law.

For requirements and effects, see question 11. Additional relief in bankruptcy is as follows:

- the debtor's incapacity to keep possession of, dispose of and administer assets is declared;
- possession and administration of assets are surrendered to the trustee;
- assets subject to the enforcement of a final judgment regarding obligations prior to the commercial insolvency declaration are excluded;
- debts to the bankrupt entity are not paid and assets shall not be surrendered to it; if debtors default, they are ordered to pay twice the amount defaulted on as a fine;
- a trustee is appointed, who shall take possession of assets and manage them; and
- in the case of an individual debtor, it is presumed that assets of a spouse acquired within two years prior to the suspect period belong to the state (the *Muciana* assumption).

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Note that there is only one insolvency proceeding, which is opened on the adjudication of the debtor in general insolvency proceedings, the same that may be opened at the stage of reorganisation or bankruptcy. The requirements for creditors placing a debtor in general insolvency proceedings in involuntary liquidation and the effects are discussed in question 11.

Involuntary petition at the stage of bankruptcy is allowed if the debtor does not oppose it, otherwise full general insolvency

proceedings shall be pursued. In involuntary bankruptcy a visit shall be conducted. There is also involuntary insolvency proceedings, under which, if the debtor and creditors fail to reach a reorganisation plan, or if the debtor does not cooperate with the plan and the conciliator (see question 11) requests a declaration of bankruptcy, the debtor is placed in liquidation.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

##### LCM overview

The LCM provides one form of insolvency proceedings that has two phases:

- conciliation (reorganisation) with the debtor in possession; and
- bankruptcy (liquidation) under the possession and administration of a trustee.

The conciliation phase may last up to 185 calendar days, with two extensions of 90 calendar days each upon the approval of a special majority of recognised creditors (first extension: two-thirds of the total debt creditors; second: 90 per cent of recognised creditors).

If no reorganisation plan is reached during the conciliation, the procedure turns into a bankruptcy (liquidation). Upon declaration of bankruptcy, assets shall be sold at public auction through a bid process. Before conciliation, there is an audit to confirm whether or not the standard for insolvency is met (see question 9).

The Federal Institute of Commercial Insolvency Specialists (IFECOM) is the trustee office and appoints:

- for the audit, an auditor who reports his or her findings accordingly to the district court (see question 9) whether the insolvency standard is met or not;
- for the conciliation, a conciliator who seeks to establish a reorganisation plan and oversees the debtor-in-possession's administration and follows the allowance claims process. The conciliator receives proof of claims and makes an allowance or disallowance proposal to court in order for it to enter a judgment on the recognition, ranking and preference of claims; and
- in bankruptcy, a trustee who possesses, administers and liquidates the estate's assets and distributes the proceeds. A trustee shall have the same powers as a conciliator in a reorganisation.

Insolvency proceedings may be voluntary or involuntary at the stage of conciliation; however, involuntary bankruptcy (liquidation) is allowed if the debtor does not oppose it. If the debtor opposes involuntary bankruptcy, conciliation proceedings are opened. Accordingly, full insolvency proceedings shall be conducted to place the debtor in involuntary bankruptcy after conciliation is exhausted. Voluntary bankruptcy (liquidation) is initiated directly upon the debtor's request.

The conditions for initiation are: the debtor must be a merchant, individual or legal entity; there are two or more creditors; and there has been a failure to make payments generally when due.

Criteria for establishing a general default on payment obligations are:

- failure to meet payment obligations to at least two creditors;
- obligations more than 30 days overdue;
- such overdue obligations represent 35 per cent or more of the total amount of the debtor's obligations as of the petition filing date; and
- the debtor must lack cash assets, as defined by the law, to pay at least 80 per cent of the total debts due as of the petition filing date. Cash assets are:
  - cash on hand and deposits on site;
  - deposits and investments due within 90 days as of the date of the petition being filed;
  - accounts receivable due within 90 days as of the date of the petition being filed; and
  - securities that regularly registered sell-or-buy operations in relevant markets, saleable within 30 banking business days.

The debtor may file a petition when it is imminent that the debtor will be under the insolvency standard in the ninety days following the petition filing (imminent insolvency).

The LCM provides for the use of standard forms issued by the Mexican Trustee's Office to speed petition filings and other motions during the proceedings.

A voluntary petition must be signed and include:

- the merchant's full name or corporate name;
- an address for notices;
- corporate and residential addresses;
- addresses of offices, facilities, establishments, plants and warehouses;
- the address of main management;
- financial statements for the past three years, audited if mandatory by law;
- a list of creditors and debtors, stating their names and domiciles, credits past due, secured and unsecured credits, priority, real or personal collateral, credits guaranteeing direct debt or third-party liabilities;
- an inventory of all assets, immoveables, moveables, securities, merchandise, stock and rights of any nature whatsoever;
- a description of legal actions to which the debtor is a party, stating the parties, identification of the proceedings, type and status;
- in the case of legal entities, the corporate decisions needed to file for general insolvency proceedings pursuant to the by-laws taken by the board of directors or the respective corporate office with legal standing for such decisions. The document must clearly show the intention of the partners or stockholders on such decision;
- the preliminary reorganisation plan offer to creditors; and
- the preliminary enterprise preservation plan.

Injunctions that may be granted before order for relief enters into effect are:

- attachment of the debtor's assets;
- order of sequestration;
- stay of executions by creditors, seizure and attachments;
- orders restraining the debtor from making payments or selling, conveying or encumbering assets; and
- transferring proceeds or securities to third parties.

General insolvency proceedings start when relief is entered, that is to say, when general insolvency proceedings is adjudicated, which creates the bankruptcy estate. Insolvency adjudication creates a special legal situation for the debtor, subject to the LCM.

The procedural effects of the general insolvency proceedings adjudication are as follows:

- opening the conciliation phase, unless the debtor has requested the bankruptcy itself or a creditor has requested it without the debtor's opposition;
- debtor is ordered to surrender its financial statements;
- debtor is ordered to cooperate and allow an auditor (visitor) and conciliator to perform their duties;
- payments are stayed, except those necessary for the ordinary course of business;
- executions and attachments are stayed, except for labour credits (salaries of the past two years);
- suspect period is set;
- summary of the order for relief is published;
- order for relief is recorded in public registries;
- notice is given to creditors to file their claim credits (proof of claims);
- proof of claims process begins; and
- a certified copy of the order of relief is issued upon request.

The substantive effects following declaration of general insolvency proceedings are as follows:

- payments are stayed, except those necessary during the ordinary course of business;
- pre-existing contractual obligations shall be performed as agreed by the parties, except for special provisions under the LCM;
- all pre-existing obligations become due and have to be fixed in UDIs (see below) to determine their amount;
- matured debts stop accruing interest. All obligations of the debtor are considered matured and interest stops accruing on obligations. However, interest will continue to accrue on obligations secured by a mortgage or a pledge even after the insolvency declarations to the extent of the collateral;

- general insolvency proceedings adjudication does not bind and lacks effect towards third-party debtors such as guarantors; and
- 2014 amendments make clear that assets that are settled under business trust (fideicomiso) are not comprised within the estate and may be separated while in the possession of the debtor, including when the debtor is the settlor.

The UDI is a unit subject to inflation adjustments, whose value is announced daily and published in the Daily Gazette of the Federation and major national newspapers.

The LCM regulates the specific pre-existing contractual obligations that may be amended when the order for relief is filed.

Performance of executory, preliminary or final contracts shall be complied with by the debtor, unless there is opposition by the conciliator, as long as it benefits the estate. The conciliator may accept or reject the contract. The other party to the contract may ask the conciliator to reject the contract. If the contract is not rejected, the debtor shall perform or guarantee the contract. If the contract is rejected, or the conciliator does not answer within 20 working days, the other party to the contract may terminate the contract at any time by giving notice to the conciliator.

### **Involuntary reorganisations**

#### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

See question 11 for conditions and qualifications.

An involuntary petition shall be signed and include:

- the court where the claim is filed;
- the claimant's full name;
- the defendant merchant's full name or corporate name and domicile, including the locations of offices, facilities, establishments, plants and warehouses;
- facts supporting the petition, stating them in a summary form with clarity and precision;
- legal standing;
- a request to declare the merchant to be in general insolvency proceedings;
- documentary evidence proving that each petitioner is a creditor;
- a guarantee for the auditor's fees if the petition is successful; and
- documentary evidence to support the claimant's action.

For effects, see question 11.

### **Mandatory commencement of insolvency proceedings**

#### **13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

Commencement of insolvency proceedings is not mandatory in any circumstances under the LCM. However, while the debtor is insolvent, as the insolvency standard is provided by the LCM, directors, key officers and officers may be liable to pay damages in favour of the debtor based upon their unlawful acts causing damages to the debtor. The LCM provides for a direct legal action that may be enforced by the debtor or stockholders holding 25 per cent of the social capital of the debtor. This action may be brought pre and post-petition. This strong damages action is independent from the voidance action available as a remedy following general insolvency proceedings adjudication. This action is also independent from a criminal liability upon general insolvency proceedings adjudication.

Directors and officers will be held personally jointly and severally liable for acts of wrongdoing. The time-bar on such action is five years.

Since most acts of wrongdoing tend to be executed while insolvent or in the suspect period, to avoid personal liability it is advisable to file for insolvency proceedings when insolvency is imminent, and especially when already insolvent.

In pre-petition, if a company carries on business while insolvent, directors and officers committing wrongdoing might be liable to indemnify damages to the debtor and may have criminal responsibility pursuant to penal laws other than the LCM.

### **Doing business in reorganisations**

#### **14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

The debtor is in possession while in conciliation proceedings and may continue in its ordinary course of business as a going concern. Assets may be used for such ends. The conciliator oversees the management of the debtor.

Creditors that supply goods and services may keep doing so. Post-petition creditors may be paid and have priority against estate assets.

Creditors may supervise the debtor by means of an interventor, who represents and protects creditors' rights and has the authority to supervise the debtor as well as to obtain information and documents from the debtor and report to the court accordingly.

The court has full authority to supervise debtors.

After insolvency proceedings are commenced by, or against, their corporation, directors and officers can exercise powers to carry on ordinary business as a going concern during conciliation.

### **Stays of proceedings and moratoria**

#### **15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

Claims being pursued by the debtor and claims against the debtor before the general insolvency proceedings adjudication shall not be joined to the insolvency proceedings, including arbitration.

Post-insolvency declaration claims, including post arbitration claims, shall not join the general insolvency proceedings. Post-insolvency claims shall be overruled by the conciliator.

Executions are stayed.

The final judgment on pre-insolvency actions shall be recognised by the insolvency court, without review, as to the amount of the claim and its priority. Claims are fixed in UDIs. Credits stop accruing interest, except secured credits up to the value of their collateral. In liquidation, secured creditors may obtain a writ of execution and be paid from the collateral.

### **Post-filing credit**

#### **16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

The LCM provides that a conciliator may approve secured and unsecured loans or credits, with new or substituted collateral, provided that the assets involved are not linked to the debtor's ordinary course of business. Court approval shall be obtained for other assets.

### **Set-off and netting**

#### **17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

Upon issuance of the general insolvency proceedings adjudication, as a general rule, offset rights no longer exist for creditors, although there are specific exceptions (eg, for post-petition creditors).

However, what was intended to be an exception has become the general rule as the law mistakenly states that, as of the date of the insolvency declaration, any legal act may be set off when a person is a debtor and at the same time a creditor of another entity, even though such debts and credits are not in cash or due yet.

Securities repurchase agreements shall be terminated upon general insolvency proceedings declaration:

- when the purchaser is declared to be in general insolvency proceedings, he or she shall convey to the seller, within 15 working days as of

- such ruling, securities of the respective kind, upon price reimbursement and payment of a premium;
- (ii) when the seller is declared to be in general insolvency proceedings, contracts shall be abandoned as of adjudication and the purchaser may claim payment of the differences in his or her favour as of the adjudication date, by means of a proof of claim, granting the seller adjudicated in general insolvency proceedings the contract price and the purchaser the ownership and securities disposition that are the subject of the securities repurchase agreement; or
- (iii) a securities repurchase agreements executed in a reciprocal way between the debtor and its counterparty shall be terminated in advance on the date of general insolvency proceedings adjudication, and shall be offset.

If there is no agreement regarding set-off and liquidation of debt balances, to make the set-off the value of the securities shall be their market value as on the adjudication date. If a verified market value cannot be determined, the conciliator may ask an experienced third party to assess their value. The outstanding balance against the debtor by virtue of their acceleration may be claimed by way of a proof of claim. If there is a balance in favour of the debtor, the counterparty shall deliver such balance to the estate within 30 calendar days of the general insolvency proceedings adjudication.

Transactions regarding loans on securities executed by the debtor with collateral in Mexican currency shall be governed like a securities repurchase agreement. Transactions regarding loans on securities executed by the debtor with collateral in securities in Mexican currency shall be governed as provided for under (iii) above regarding the securities repurchase agreements.

Differential agreements or future agreements and derivatives financial transactions that shall terminate after the general insolvency proceedings adjudication, must be terminated in advance of the adjudication. Such contracts and transactions shall be set off under the LCM. In the case of silence, for the set-off and liquidation of debt balances to make perform set-off, the value of the goods and underlying obligations shall be that of their market value as on the adjudication date. If a verified market value cannot be determined, the conciliator may ask an experienced third party to assess their value.

After the set-off is made, the balance of the debt may be claimed by the creditor by way of a proof of claim (ie, by means of the set-off the debt is accelerated and becomes due and payable). If there is a balance in favour of the debtor, the counterparty shall deliver such balance to the estate within 30 calendar days of the general insolvency proceedings adjudication.

For purposes of the LCM, transactions that parties of a contract have made that are bound to the payment of money or the fulfilment of other obligations to supply items or services with a market good or value as will be understood as financial derivatives, as will any agreement that by general regulation is indicated by the Bank of Mexico. It shall be set off and shall be due and payable under the contractual terms or as provided for under the LCM.

As of the date of the general insolvency proceedings adjudication, debts and credits that may be given a monetary value regarding any of the following may be made due and payable under the LCM, even if such debts and credits are not due and payable as of the date of the general insolvency proceedings adjudication:

- framework agreements;
- regulatory agreements;
- specific agreements executed regarding:
  - derivative financial transactions;
  - securities repurchase agreements;
  - transactions of loans on securities;
  - transactions on futures; or
  - any equivalent transaction; or
- any other juridical acts in which one person is a debtor of another and at the same time is a creditor such other entity.

The outstanding balance from the set-off against the debtor may be claimed by way of a proof of claim. If there is a balance in favour of the debtor, the counterparty shall deliver such balance to the estate within 30 calendar days as of the general insolvency proceedings adjudication.

## Sale of assets

### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

The insolvency regime does not provide for stalking horse bids in sales procedures. Sales are made in court auction sales. The court may authorise other proceedings to optimise sales to benefit the estate. Purchases acquire the assets 'free and clear' of claims.

A creditor may make payment of the purchase price only with court-approved distributions. A creditor may not make payment of such purchase price by reducing the amount of a claim (allowed claim).

The court may not allowed assessing credit bid since creditors may pay with court-approved distributions.

The assignee of the original secured creditor, provided assignment is summoned to court, has legal standing to participate in the bid as successor of the original secured creditor.

## Reorganisation

During conciliation, the debtor remains in possession of the assets and may continue day-to-day operation of the business. The debtor's limited performance, business and accounting are under the conciliator's supervision.

The conciliator shall decide on the rescission of pending contracts (see question 21).

The conciliator shall, having consulted the administrator (see question 14), approve post-petition financing, the grant or substitution of collateral (with the creditor's approval) and asset transfers that are non-essential to the business; the conciliator shall report to the court accordingly.

The conciliator may perform direct transfers if goods are perishable, will suffer a strong price diminution or will incur a high maintenance cost; the conciliator will report to the court accordingly.

The conciliator and debtor must keep the business as an ongoing concern. However, to benefit the estate, the business may be closed, totally or partially, temporarily or permanently, to prevent the debt increasing or deterioration of the estate.

With court approval, assets may be sold.

While debtor in possession, the conciliator may call meetings of the board of directors, the council, committees or stockholders for corporate decisions.

The debtor may be suspended from administration of the bankruptcy estate, if the conciliator considers it necessary. The conciliator shall administer the estate with the same powers as those given to the trustee in a liquidation.

The power of the board of directors, stockholders' meetings or similar legal entities to decide on the appointment or dismissal of conciliators, directors or managers shall be suspended (stay).

Assets not linked for the carrying on of the business as a going concern and sales that benefit the estate may be sold by the conciliator with or without court approval, provided that sales of assets rules under the LCM are followed.

## Liquidation

Assets shall be sold by public auction. Such sale shall seek the maximum price whether by sale of the entire business, parts of the business or its assets.

Upon the court's approval, assets may be sold in a different process from public auction for a better sale price than would be obtained by public auction.

The trustee may sell assets immediately if they might deteriorate, diminish in value or involve a high cost of maintenance in proportion to their value. To maximise the sale price, the entire business of the debtor may be improved as an ongoing concern. If not, assets may be sold in packages to facilitate the sale. The sale shall be free and clear of claims.

The bid shall indicate the minimum price, which is equivalent to stalking horse bids.

Credit bidding in sales is permitted for creditors holding the specific right to receive a dividend for a sale.

Securities and stock may be sold without applying the Securities Law regarding securities offers.

Assets subject to a separation claim may not be sold until dismissal of the final claim.

The sale shall be conducted even if proof of claims is still pending.

It should be noted that LCM prevents the lowering of the value of the assessed assets.

During the first 30 calendar days of the bankruptcy stage, the trustee may only prevent a separate collateral foreclosure on assets linked to the ordinary operation of the enterprise when the trustee considers that it benefits the estate by sealing it in conjunction of assets.

### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

Opening of insolvency proceedings does not prevent the execution of an IP licence agreement.

The conciliator in reorganisation (conciliation) and trustee in liquidation may oppose execution and may terminate such licences.

A party may ask a conciliator or trustee whether or not it will oppose execution. If there is no response, a licence may be terminated.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Federal Law on Personal Information Protection in Possession of Private Persons, enacted on 5 July 2010, provides for the protection and privacy of personal information or customer data. It, generally, prevents use or transfer of personal information and customer data without the owner's agreement. However, if the owner does not expressly oppose the privacy notice of the person to whom it is given, it is assumed that the owner tacitly agrees that his or her personal data may be used or transferred as it is provided for under the privacy notice. In insolvency proceedings, personal information and customer data may be used or transferred as long as it is within the scope of the privacy notice. There are some exceptions under some circumstances to use or release this information or these data under this Law.

### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

The LCM regulates specific pre-existing contractual obligations that may be amended when the order for relief is entered.

Performance of executory, preliminary or final contracts shall be complied with by the debtor, unless there is opposition by the conciliator, as long as it benefits the estate. The conciliator may accept or reject the contract. The other party to the contract may ask the conciliator to reject the contract. If the contract is not rejected, the debtor shall perform or guarantee the contract. If the contract is rejected, or the conciliator does not respond within 20 working days, the other party to the contract may terminate the contract at any time giving notice to the conciliator. When the conciliator is in charge of administration or authorises the debtor to perform contracts, upon payment of the costs the conciliator may prevent assets being separated or claim delivery of assets.

If a debtor breaches the contract after the insolvency case is opened, the conciliator may enforce legal action seeking mandatory

contract fulfillment or termination thereto – in either case with payment of damages.

For purchase and sales agreements, to claim delivery of assets, moveable or immovable, the price shall be paid or a guarantee provided to the seller.

Sellers of goods in transit at the time of the general insolvency proceedings adjudication and not yet delivered to the debtor may oppose delivery, either by modifying the consignment as permitted by law or by materially stopping delivery. Such matters shall be pursued between the seller and debtor in discussions with the conciliator's participation.

A seller of real estate who is declared to be in general insolvency proceedings may deliver real estate upon payment of the price, provided the sale is legally perfected.

A buyer that is declared to be in general insolvency proceedings, upon payment of such price or receiving a guarantee thereof, may enforce delivery of goods. If delivery was made under a sale agreement, the seller may repossess the goods if the sale was not formalised by a public instrument, where provided by law.

If enforcement is decided upon and a purchase and sale agreement was made stating that payment for the goods was payable at a future date, the seller may claim a fulfilment guarantee.

If the claim relates to the sales of goods that are delivered over a period of time and some deliveries have been made, such deliveries shall be paid for. If it is decided to enforce this agreement, the price for the remaining deliveries must be guaranteed to the seller.

If the seller of a moveable asset is declared to be in general insolvency proceedings, if the assets had been identified before adjudication, the buyer may enforce fulfilment of the delivery upon payment for the asset.

A deposit agreement, revolving line of credit agreement, commission agency agreement and mandate agency agreement may not be terminated by adjudication in general insolvency proceedings of any party, unless the conciliator terminates them.

Current accounts, upon general insolvency proceedings adjudication, shall be terminated and shall be liquidated to claim any balance therein, unless the debtor, with the conciliator's approval, is permitted to continue the current accounts.

Securities repurchase agreements shall be terminated upon general insolvency proceedings declaration:

- (i) when the purchaser is declared to be in general insolvency proceedings, he or she shall convey to the seller, within 15 working days as of such ruling, securities of the respective kind, upon price reimbursement and payment of a premium;
- (ii) when the seller is declared to be in general insolvency proceedings, contracts shall be abandoned as of adjudication and the purchaser may claim payment of the differences in his or her favour as of the adjudication date, by means of a proof of claim, granting the seller adjudicated in general insolvency proceedings the contract price and the purchaser the ownership and securities disposition that are the subject of the securities repurchase agreement; or
- (iii) a securities repurchase agreements executed in a reciprocal way between the debtor and its counterparty shall be terminated in advance on the date of general insolvency proceedings adjudication, and shall be offset.

If there is no agreement regarding set-off and liquidation of debt balances, to make the set-off the value of the securities shall be their market value as on the adjudication date. If a verified market value cannot be determined, the conciliator may ask an experienced third party to assess their value. The outstanding balance against the debtor by virtue of their acceleration may be claimed by way of a proof of claim. If there is a balance in favour of the debtor, the counterparty shall deliver such balance to the estate within 30 calendar days of the general insolvency proceedings adjudication.

Transactions regarding loans on securities executed by the debtor with collateral in Mexican currency shall be governed like a securities repurchase agreement. Transactions regarding loans on securities executed by the debtor with collateral in securities in Mexican currency shall be governed as provided for under (iii) above regarding the securities repurchase agreements.

Differential agreements or future agreements and derivatives financial transactions that shall terminate after the general insolvency proceedings adjudication, must be terminated in advance of the

adjudication. Such contracts and transactions shall be set off under the LCM. In the case of silence, for the set-off and liquidation of debt balances to make perform set-off, the value of the goods and underlying obligations shall be that of their market value as on the adjudication date. If a verified market value cannot be determined, the conciliator may ask an experienced third party to assess their value.

After the set-off is made, the balance of the debt may be claimed by the creditor by way of a proof of claim (ie, by means of the set-off the debt is accelerated and becomes due and payable). If there is a balance in favour of the debtor, the counterparty shall deliver such balance to the estate within 30 calendar days of the general insolvency proceedings adjudication.

For purposes of the LCM, transactions that parties of a contract have made that are bound to the payment of money or the fulfilment of other obligations to supply items or services with a market good or value as will be understood as financial derivatives, as will any agreement that by general regulation is indicated by the Bank of Mexico. It shall be set off and shall be due and payable under the contractual terms or as provided for under the LCM.

As of the date of the general insolvency proceedings adjudication, debts and credits that may be given a monetary value regarding any of the following may be made due and payable under the LCM, even if such debts and credits are not due and payable as of the date of the general insolvency proceedings adjudication:

- framework agreements;
- regulatory agreements;
- specific agreements executed regarding:
  - derivative financial transactions;
  - securities repurchase agreements;
  - transactions of loans on securities;
  - transactions on futures; or
  - any equivalent transaction; or
- any other juridical acts in which one person is a debtor of another and at the same time is a creditor such other entity.

The outstanding balance from the set-off against the debtor may be claimed by way of a proof of claim. If there is a balance in favour of the debtor, the counterparty shall deliver such balance to the estate within 30 calendar days as of the general insolvency proceedings adjudication.

A lessor adjudicated in general insolvency proceedings shall not terminate a lease agreement on real estate. A lessee adjudicated in general insolvency proceedings shall not terminate a lease agreement on real estate. Notwithstanding the above, the conciliator may elect to terminate the agreement, in which case the lessor shall be paid the contractual indemnity. If there is no other agreement made, payment of three months of rent for the acceleration must be made.

Service supply agreements of a strictly personal nature shall be binding over the parties and shall not be terminated.

Lump-sum construction contracts shall be terminated upon general insolvency proceedings of any party, unless the party adjudicated in general insolvency proceedings, with the authorisation of the conciliator, agrees to fulfil the contract with the other party.

Insurance entities adjudicated in general insolvency proceedings may not terminate insurance contracts over real estate. In the case of moveables, the insurer may terminate the insurance contract.

If the conciliator fails to notify an insurer that an entity insured by it has been adjudicated in general insolvency proceedings within 30 days of the adjudication, the insurance contract shall be terminated, effective as of such adjudication.

Regarding life insurance contracts or mixed contracts, the debtor, with the conciliator's authorisation, may decide on the assignment of the insurance bond and obtain a reduction of the insured capital, in proportion to the premiums already paid pursuant to calculations that the insurance company has taken into account and considering also the risks covered by it. Likewise, the debtor may make any other transaction that economically benefits the estate.

There are specific requirements for the general insolvency proceedings adjudication of:

- a partner of a general partnership (unlimited liability partnership);
- a partner of a limited responsibility partnership;
- a general partner (unlimited liability partnership) of a limited liability partnership company; or

- a general partner (unlimited liability partnership) of limited liability stock partnership company.

Such partner, in each case, is entitled to request its liquidation as of the last company balance sheet or to continue being a partner to the company, if the conciliator so agrees. However, the remaining partners may instead choose to exercise their right to partially liquidate the company, unless the company's by-laws state otherwise.

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#### Arbitration processes in insolvency cases

##### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

There is no arbitration in insolvency matters. Insolvency, as a mandatory proceeding according to public policy, is under the exclusive federal jurisdiction of the state and not subject to arbitration. Accordingly, disputes arising in insolvency cases after they have been opened may not be arbitrated, even if both parties agree to arbitrate the dispute. The LCM provides that late actions shall not be joined to the general insolvency proceedings. The general insolvency proceedings court may not refer parties to arbitration. In theory, pre-petition insolvency cases may be subject to arbitration if all creditors and the debtor agree on the arbitration. The LCM is silent as to arbitration processes in insolvency cases. It is desirable that the LCM provides for arbitration.

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#### Successful reorganisations

##### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

The LCM favours rehabilitation of the enterprise, and liquidation only takes place when rehabilitation is impossible. A reorganisation plan requires a simple majority of more than 50 per cent approval of approved creditors.

The conciliation phase is intended to create the best conditions for a reorganisation plan. The LCM does not regulate terms or conditions for the plan, but only sets forth minimum rules to ensure the legality of the plan. The LCM, however, provides mandatory notices and access to information to enable interested parties to exercise and protect their rights. Accordingly, the conciliator may recommend that appraisals and studies be conducted when they are necessary to achieve a reorganisation plan, as would be given to creditors through the court. When the conciliator considers that there is an agreement of a simple majority of more than 50 per cent of the recognised creditors in the plan, he shall give the plan to the other recognised creditors to give their opinion thereon or to execute the plan.

In order to approve a viable reorganisation plan that favours all or most creditors under the circumstances, the LCM provides mechanisms to protect the rights of minority creditors by giving them most favourable terms under the plan. This thereby avoids unnecessary or burdensome objections by minorities that in fact benefit from the plan.

Only those creditors with accepted claims may agree on the plan. Labour and tax creditors do not execute the plan. To facilitate approval of the plan, unsecured, subordinated and participating secured creditors shall be taken into account for determining the necessary majority.

The reorganisation plan, regarding non-participating creditors holding recognised debt, may only provide extension of time to pay the debt or debt discount or combination of both, provided that terms and conditions are equal to those agreed by at least 30 per cent of creditors holding unsecured allowed claims.

The plan may provide for an increase of capital. Shareholders must be notified in order to exercise first refusal rights. If shareholders do not exercise their rights, the court may approve the capital increase.

Dissenting recognised unsecured creditors holding a simple majority or recognised unsecured creditors holding 50 per cent of the debt may veto the plan proposal. If there are no objections, the plan may be approved by the court. Since the approved plan is binding upon absent

and dissenting creditors, the most favourable terms and conditions of the plan shall be allocated to them.

The plan shall be approved by more than 50 per cent of allowed creditors (unsecured, subordinated and secured) executing the plan.

Upon the court's approval of the plan, the insolvency process terminates and parties cease to perform their functions.

The plan shall provide payment for:

- labour creditors (highest priority);
- creditors (administration costs and fees of the insolvency estate) whose claims are secured by assets of the estate;
- claims for burial costs when death is pre-general insolvency proceedings;
- claims for costs of sickness that caused the death of the debtor when death is post-general insolvency proceedings;
- secured creditors with mortgage or pledge;
- claims holding special privilege pursuant to law;
- tax credits; and
- fund for challenged claims and tax credits that have not been determined.

Private agreements between the debtor and any creditor are null and void once relief is granted and the creditor shall lose such rights.

The plan may not release non-debtor parties, such as guarantors. The plan may only bind a debtor and its creditors. However, the liabilities of officers, directors, advisers and lenders may be released in writing by the interested party or parties taking legal action against them.

The approved plan binds debtor, all creditors holding subordinated allowed claims, creditors holding secured allowed claims, who executed the plan or creditors holding secured allowed claims for whom the plan provides for full payment as of the general insolvency proceedings adjudication.

For voting of intercompany claims, see question 43.

#### **Mandatory enforcement of the restructuring plan**

Any allowed creditor may request the mandatory enforcement of the restructuring plan by means of a summary proceeding before the court that adjudicated the commercial insolvency.

#### **Amendment of the plan**

In the case of a change of circumstances that materially affects the fulfilment of the plan, it may be amended in order to satisfy the need to preserve the enterprise.

#### **Expedited reorganisations**

##### **24 Do procedures exist for expedited reorganisations?**

A pre-packaged reorganisation is allowed by agreement between the debtor and creditors holding a simple majority of more than 50 per cent of the total debt. The debtor and creditors will execute the petition. It is required that the debtor states under oath that it is already in a state of insolvency and explains why, or states that such insolvency is imminent within 90 working days and that the creditors signing the petition hold at least a simple majority of more than 50 per cent of the total debt. The proposed reorganisation plan must be enclosed with the petition. A full insolvency proceeding will be followed without an audit. Protection measures and stays may be requested and granted upon filing of the petition. The court must approve the plan, whereupon the proceeding ends.

#### **Unsuccessful reorganisations**

##### **25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

No executing recognised creditors may defeat the plan if due process for the plan is not met and if mandatory plan standards are not met. Due process includes access to supporting information and plan viability as well as full knowledge of the plan terms and conditions.

A majority of unsecured creditors whose proofs of claim have been allowed may veto the plan. Unsecured creditors not signing the plan may not object to the plan if they are to be paid in full.

Court approval of a plan may be appealed, without stay. A successful appeal dismissing the plan on legal grounds is sent to court. A new plan may be proposed. Otherwise, the case turns into a liquidation.

A default on the plan by the debtor turns the case into a liquidation.

#### **Insolvency processes**

##### **26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

Meetings may be called by court order with notice by means of personal service, court list publication at the court door, the daily gazette of the federation or newspapers. In general, all such information and documents are available to them, except restricted information and documents protected by legal secrecy and confidentiality.

In addition, upon the request of the interventors, creditors may have access to the debtor and estate information that may affect creditors' rights.

Trustees shall provide court and interventors' reports every two months.

Domestic and foreign creditors with known addresses are notified personally of the insolvency opening. All creditors are notified by publication of a notice in the daily federal gazette and a major newspaper. There are no mandatory meetings, although meetings may be held. There are no mandatory committees.

Creditors may request a trustee or interventor to enforce remedies against third parties. Creditors may enforce remedies as an action of subrogation.

A reorganisation plan may not provide for release of liabilities owed by third parties who are not part of the debtor group. The LCM prevents that third party debtor remains liable.

#### **Enforcement of estate's rights**

##### **27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

There is an action for subrogation by means of which creditors may enforce claims available to the estate. The fruits of such actions belong to the estate. Creditors are entitled to be reimbursed for their costs. The creditor may enforce its debtor's rights against this latter debtor's debt.

#### **Creditor representation**

##### **28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

Within the insolvency proceeding, creditors may be represented by interventors who oversee the trustee's performance and may obtain from the debtor or trustee a review of information that may affect creditors' rights.

Creditors are free to form their own committees and it is a regular practice to form committees outside the insolvency proceeding.

Advisers may be appointed by creditors and costs are funded or borne by them.

#### **Insolvency of corporate groups**

##### **29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

The LCM now regulates groups of companies, and there is no piercing of the corporate veil. The LCM provides that the insolvency proceeding of holding and subsidiary companies will be joint in the same commercial insolvency proceeding, but each company's insolvency will be conducted in a separate court docket file. The LCM does not provide for these to be combined or consolidated for administrative purposes, nor may their assets or liabilities be pooled for distribution. However, creditors or debtors of the same group of companies may file for joint

commercial insolvency as far as one or more of the enterprises of the same group of companies meet the insolvency standard. The court may appoint the same visitor, conciliator or trustee, should it benefit the proceedings.

Mexican corporate law does not provide for the insolvency of corporate groups. Corporate groups consolidate for tax purposes. Labour law recognises a substitute employer among a group of companies. The Law on Financial Groups provides for financial groups of companies, with joint and several liabilities without consolidation. Regarding groups of companies, assets may not be transferred from an administration in Mexico to another country.

### Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

The rights to appeal are to challenge a court order seeking its amendment or reversal based upon an appellant's opinion that the court order is unlawful. An appellant has an automatic right to appeal. Under the Commercial Insolvency Statute, there is no stay of the court order under appeal. There are just a few court orders that may be appealed, such as the judgment adjudicating debtor in concurso mercantil, the judgment on the recognition, ranking and priority of claims and the judgment adjudicating the debtor in bankruptcy. There is an extraordinary remedy, namely *amparo* action, by means of which decisions of the appeal may be further challenged before a constitutional court. In the insolvency proceedings, most court orders may be challenged by a remedy, namely revocation, which is decided by the same court presiding the insolvency proceeding.

### Claims

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

There is a written format for proofs of claim that must be attached to either the original or a certified copy of documentary evidence. A certified statement of account and accounting expert opinion may be filed to support the claim. If they are issued abroad, they shall be ratified before a notary public and apostilled. Note that a claim may be signed by an officer of the creditor; however, a valid and enforceable power of attorney may be needed. This format is found at [www.ifecom.cjf.gob.mx](http://www.ifecom.cjf.gob.mx). Proofs of claim shall be filed before the period for appealing the judgment has expired.

Disallowed claims are announced alongside the judgment of which claims have been allowed. Such dismissed claims may be challenged by appeal. Claims may be transferred, which must be notified to the court. Private agreements between the debtor and any creditor are null and void once relief is granted and the creditor shall lose such rights.

To participate in the discussion, approval, agreement and veto of the plan, creditors must hold approved claims.

A claim acquired at a discount may be enforced for its full face value. Acquisition shall be notified to court, debtor, conciliator and trustee.

Interest that accrued after the opening of an insolvency case may not be claimed by a creditor except on secured claims up to the collateral value.

Claims for contingent or unliquidated amounts shall be determined by final judgment rendered by a court outside the general insolvency proceedings.

### Modifying creditors' rights

**32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

Modifying creditors' rights is not provided for under the LCM.

### Priority claims

**33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Administration and conservatory claims of the estate have priority over secured creditors. However, these claims have no priority over labour claims and tax claims. Claims on burial when death is pre-insolvency and claims on illness when death is post-insolvency have priority over secured claims.

### Government

Tax creditors, whether federal, state or municipal, social security credits (IMSS) and INFONAVIT credits have priority. These tax credits have priority over secured creditors, provided such tax credits are determined and notified before the date of the collateral of secured creditors.

### Non-governmental

Labour credits have super-priority over secured creditors and tax creditors.

### Employment-related liabilities in restructurings

**34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

Employment contracts may be terminated upon general insolvency proceedings or bankruptcy adjudication when the court or creditors decide on total closure of the business or reduction of work. Notice must be given to the labour court, which in a special labour proceeding may allow or disallow such termination or reduction. Workers are entitled to receive three months' salary and 12 days' salary per year of employment (seniority bonus). Labour claims on pension funds may be regarded as an indemnity in favour of the workforce and accordingly such claims may have labour-claim priority.

### Pension claims

**35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Labour matters are not subject to LCM jurisdiction even in the context of an insolvency. An employee's labour claim is not joined to a general insolvency proceedings, so remedies for pension-related claims against employers must be asserted before the labour courts. Labour rights and claims are super priority claims, and the court may enforce its judgment over employers' assets, and attach or auction them to satisfy claims.

Actuarial deficiencies in pension assets and unpaid contributions to employee pension plans both give rise to claims that may be asserted before the labour courts.

### Environmental problems and liabilities

**36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

Environmental problems and liabilities are dealt by the official agencies and special laws thereto. The debtor is directly responsible for controlling the environmental problem and for remediating the damage caused. Official environmental agencies make an overview of the problem and then instruct the debtor to control the environmental problem and remediate the damage caused. Federal congress may also participate. The insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, and third parties may be liable for environmental responsibility, including indemnity for damages.

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**Liabilities that survive insolvency proceedings**


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**37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

Government tax credits and labour credits survive insolvency proceedings and are enforceable, unless otherwise provided by agreements of labour and tax creditors under the plan. An insolvency court may not assert jurisdiction over tax and labour creditors.

In a reorganisation plan, liabilities may survive unless it is agreed that they are fully discharged. There are no dischargeable debts.

There is no discharge in liquidation. If payment is not made in full, liabilities survive and creditors may enforce the outstanding balance of the claim.

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**Distributions**


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**38 How and when are distributions made to creditors in liquidations and reorganisations?**

Distributions are made in the liquidation phase with proceeds realised from the sale of estate assets. Distribution is made pursuant to a proof of claims judgment. In reorganisations, distribution is made pursuant to the plan.

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**Transactions that may be annulled**


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**39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

In general, all fraudulent transactions executed against creditors and the insolvency estate may be set aside.

The LCM defines as felonious those fraudulent acts that cause or aggravate the cessation of payments, as provided by law. These acts may be set aside as well.

Fraudulent transactions performed during the suspect period that may be annulled include:

- gratuitous acts, transactions with no consideration;
- acts and disposals in which the debtor pays an excessive consideration, or receives consideration whose value is lower than the goods or services supplied by its counterparty;
- transactions carried out by the debtor in which conditions or terms were agreed upon that are significantly different from the conditions prevailing in the market in which the transactions were carried out on the date on which they were carried out, in which or the terms differed significantly from trade usage or practices;
- debt remission or write-off;
- payment of obligations not due; and
- discount of debtor's own notes by the debtor, which will be regarded as a prepayment.

Voidance may not be granted if the estate benefits from the payments made to the debtor. If the third party returns whatever it received from the debtor, it may request the recognition of its credits.

Fraudulent acts performed during the suspect period, unless the debtor's counterparty proves its good faith, include:

- creation of guarantees or the increase of any existing guarantees, if the original obligation did not contemplate such guarantee or increase; and
- any payments of debts made in kind, if the later is different from that originally agreed upon or if the agreed-upon consideration was in cash.

All acts performed during the suspect period by the debtor with relatives or related individuals or legal entities may be regarded as fraudulent and voidable.

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**Proceedings to annul transactions**


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**40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

In general, all fraudulent transactions executed against creditors and the insolvency estate may be set aside. The LCM defines as 'felonious' those fraudulent acts that cause or aggravate the cessation of payments, as provided by law. Such acts may also be set aside.

Fraudulent or preferential acts may be reviewed and declared void. The LCM prescribes a 270-calendar-day 'suspect period' to be reviewed, counting backwards from the date the order for relief was made. This term may be doubled in the case of related subordinated creditors (intercompany or insiders' debt). A request for a longer review period of up to three years must be filed before the judgment on recognition, ranking and priority is entered. The burden to prove is more flexible to obtain extension of the suspicious period without need to prove the actual fraud, which is a separate cause of action. The new retroactive period must be announced by publication in the court's list of orders.

Voidable transactions may be challenged by creditors and the trustee. Voidance actions, like civil or criminal actions, involve lengthy litigation and are often costly.

**Directors' and officers' liability regime**

Legal standing to enforce actions seeking civil liability (damages) when upon fraudulent transactions (voidance actions) may be brought by: one-fifth or more of the allowed creditors; allowed creditors that jointly represent 20 per cent of the total allowed credits; interventors; the debtor; and shareholders holding 25 per cent of the debtor's shares. The time-bar on damages actions is five years.

In the context of an insolvency proceeding, the LCM now provides a regime of strict civil and criminal liability for the debtor, debtor's general director, sole administrator, board of directors, legal representatives and key employees, including insiders and relatives when causing damages in regard to the facts and circumstances provided by the LCM. Damages shall be to the benefit of the estate. Civil liability is joint and several and is independent from criminal liability, which may be from three to 12 years' imprisonment.

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**Directors and officers**


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**41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

Criminal responsibility shall be borne by the debtor. In the case of a legal entity, such responsibility will be borne by its board of directors, management or liquidators. They may be liable for pre and post-bankruptcy.

If new management is appointed and they discover felonies or misbehaviour, the new administration shall report it, otherwise its members will become liable.

In the case of tax fraud or tax default, the new management shall report it. Otherwise, they are liable to pay it. In a limited liability partnership, corporate law prevents partners from taking management roles. A default makes them jointly and severally liable towards contracting third parties. The law also provides that general partners are jointly and severally liable for the partnership's business.

Directors and officers involved in fraud are liable. Directors and officers may be liable if, knowing of misbehaviour or felonies regarding former administrators or officers, they do not report it. Default on obligations makes them jointly and severally liable towards contracting third parties. In a limited liability stock partnership, the law provides that general partners are jointly and severally liable for the partnership's business.

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**Groups of companies**


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**42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

The LCM now regulates groups of companies, and there is no piercing of the corporate veil. The LCM provides that the insolvency proceeding

of holding and subsidiary companies will be joint in the same commercial insolvency proceeding, but each company's insolvency will be conducted in a separate court docket file. The LCM does not provide for these to be combined or consolidated for administrative purposes, nor may their assets or liabilities be pooled for distribution. However, creditors or debtors of the same group of companies may file for joint commercial insolvency as far as one or more of the enterprises of the same group of companies meet the insolvency standard. The court may appoint the same visitor, conciliator or trustee, should it benefit the proceedings.

Mexican corporate law does not provide for the insolvency of corporate groups that are consolidated for tax purposes. Labour law recognises a substitute employer among a group of companies. The Law on Financial Groups recognises for financial groups of companies with joint and several liabilities without consolidation. In such groups, assets may not be transferred from an administration proceeding in Mexico to one in another country.

Parent or affiliated corporations may be responsible for the liabilities of subsidiaries or affiliates when they are legally linked by virtue of a guarantee or a similar obligation to act with respect to the subsidiaries or affiliates. All of them are considered independent legal entities with independent patrimonies. Their being related companies does not make them liable for the liabilities of the others.

A court may not order a distribution of group company assets *pro rata* without regard to the assets of the individual corporate entities involved since the estates do not merged and are not pooled.

Separation action may be enforced to recover assets or rights belonging to the debtor's estate.

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### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

As a reaction to the well-known *Vitro* case, the 2014 amendments of the LCM now provide for 'intercreditors debt' (subordinated debt) providing for a new ranking of creditors holding subordinated debt, namely subordinated creditors, that may be created by:

- contractual agreement or provided by statute law;
- the unsecured intercompany and insiders debt; except for claims of a parent company and individuals that only have control over the debtor for claims ranking. This exception does not include, *inter alia*, casting votes for the reorganisation plan or fraudulent conveyances; and
- late-claim filings.

In order to prevent fraudulent conveyance of intercompany indebtedness and to give certainty to investors and creditors that their debt would be paid first before certain intercompany obligations, the 2014 amendment provides that in case the debtor is a corporation, the following unsecured creditors (statutory insiders) shall be characterised as subordinated in ranking:

- (i) subsidiaries and affiliates of the debtor;
- (ii) the director, members of the board of directors and key officers of the debtor, as well as those of its subsidiaries and affiliates; and
- (iii) corporations with the same managers, members of the board of directors or key officers similar to those of the debtor (commonality of management).

In the event the insolvent company is put into liquidation, all of the aforementioned creditors shall receive payment only after senior debt claims are paid in full. Claims held by controlling individual shareholders and by the holding company of the debtor were excluded from subordination in payment as lawmakers considered that including such claims would impair their ability to obtain financing from lenders.

#### Voting of 'intercompany' claims

In an inter-company claim, there may be no cram down of legitimate third-party claims on the basis of an inter-company or insider-debt casting vote. The plan must be agreed by the debtor; creditors representing more than 50 per cent of the sum of all the debtor's unsecured and subordinated claims; and creditors representing more than 50 per cent of the debtor's secured or priority creditors.

Further, if inter-company claim holders and insiders (including controlling individual shareholders and holding companies) as subordinated creditors, hold at least (jointly or severally) 25 per cent of the total amount of the credits of (i) and (ii), above, then to become effective, the plan must be accepted by creditors representing at least 50 per cent of such credits, excluding from this amount the claims of the insiders.

This rule will not apply when inter-company claim holders and insiders accept the plan as agreed by the rest of the voting claim holders, in which a case the simple majority rule apply.

Now, the voting of insider or inter-company claims together with third-party claims will only be sufficient to approve a reorganisation if at least half of the non-insiders vote in favour of the plan.

#### Subordinated debt and 'subordinated creditors'

Creditors' agreements may provide for the total or partial extinction of subordinated debt or other type of treatment thereto, including its subordination or another form of particular treatment.

#### Interaction before the Mexican courts of indenture trustees and bond holders

Proof of claims may be filed individually by a bond holder, which will be subtracted from the overall proof of claim filed by an indenture trustee representing bond holders. Each bond holder as well as the trustee is entitled to pursue allowed claims, rights, objections and voting rights.

Bond holders' meetings shall be conducted as provided under the indenture agreement, the law governing the indenture or by the LCM; the decisions of bond holders' meetings will have a binding effect.

#### The extinction of debts

The restructuring plan and the judgment approving it shall be the only document governing the debtor's obligations towards allowed creditors.

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### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Processes for seizure of assets include:

- tax enforcement by attachment or seizure;
- criminal seizure in case of felony;
- labour executions by attachment; and
- seizure by customs authorities.

In all these cases, attached assets may be foreclosed and sold.

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### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

The Law on Corporations provides for the private out-of-court corporate dissolution and liquidation of a company. In essence these are very similar: liquidation of assets to pay creditors. If there is any balance remaining it goes to stockholders. Corporate liquidation does not provide for court orders to stay payments and executions. Liquidators may apply for voluntary general insolvency proceedings.

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### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Reorganisation concludes with court approval of the plan. Liquidation concludes with the sale of estate assets and payment of creditors' claims up to their sale proceeds. There is a court judgment declaring termination.

#### Conditions for termination of insolvency proceedings

- (i) The reorganisation plan may be approved by simple majority of creditors holding allowed claims. In liquidation, the plan must be approved by such creditors and the plan provides payment for all creditors holding allowed claims, including those not executing the plan;
- (ii) full payment of recognised claims is made;

- (iii) recognised claims are partially paid and there are no estate assets left to liquidate;
- (iv) it is proven that the estate assets are not sufficient to pay expenses and fees for the administration of the estate; or
- (v) proceeding can be terminated at any time upon request of the debtor and all recognised creditors.

#### Reopening of commercial insolvency proceedings

In the case of (iv) or (v) above, proceedings may be reopened if it is proven that in the two years following termination there are assets to pay at least the expenses and fees for the administration of the estate.

Termination is made upon court judgment.

The LCM does not provide for discharge in liquidation.

#### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

Mexico has incorporated the UNCITRAL Model Law on Cross-Border Insolvency. Accordingly, Mexico provides recognition and full cooperation on cross-border insolvency. Foreign creditors are granted equal treatment with domestic creditors. The federal judiciary has granted relief sought in support of the Model Law.

Mexico was the first jurisdiction to recognise two foreign bankruptcy proceedings under the Model Law and grant international insolvency cooperation thereto – the *Xacur* case and the *IFS* case.

Mexico has no international treaty on insolvency, bankruptcy or reorganisation matters. Mexico has executed two treaties on the recognition of foreign judgments that expressly exclude insolvency, reorganisation, bankruptcy and liquidation.

The LCM incorporates the UNCITRAL Model Law in Chapter 12. The law defines the following terms:

- ‘foreign proceedings’ – collective judicial or administrative proceedings in a foreign country, including interim proceedings, under a law relating to insolvency, or adjustment of debt proceedings in which the assets and affairs of the debtor are subject to control or supervision by a foreign court, for the purpose of reorganisation or liquidation;
- ‘main foreign proceedings’ – foreign proceedings pursued in the jurisdiction where the debtor’s centre of main interest (COMI) is located;
- ‘foreign representative’ – a person or body, including provisional persons or bodies, empowered in foreign proceedings to administer the reorganisation or liquidation of the debtor’s assets and affairs or to act as a representative of foreign proceedings;
- ‘foreign court’ – a judicial authority or other body with jurisdiction over the control or supervision of foreign proceedings; and
- ‘establishment’ – any place of operations where the debtor carries out a non-transitory economic activity with employees and goods and services.

Reciprocity is mandatory. International cooperation may be conducted through Mexican courts and Mexican representatives. Foreign courts and foreign representatives may only act through a Mexican court or Mexican representative. Recognition is not automatic. If a debtor has an establishment in Mexico, full insolvency proceedings (general insolvency proceedings) under the LCM shall be conducted. Otherwise, foreign proceedings may be recognised in summary proceedings. In interpreting and applying Chapter 12, consideration shall be given to avoiding any violation of the LCM and current prevailing fundamental principles of law in Mexico. Please note that Chapter 12 allows the rejection of recognition when there is any violation whatsoever of the LCM or any of such fundamental principles of Mexican law. Thus, Chapter 12 mandates, for overwhelming reason, rejection when there is a manifestly violation of public policy. Protection measures (stay of payments or execution) may be granted following the request being filed

for recognition. Upon recognition, additional protective measures may be granted. Foreign proceedings shall be recognised as main or non-main proceedings, subject to the debtor’s COMI. Chapter 12 shall be interpreted considering its international origin and the need to promote uniformity in its application and good faith observance. Chapter 12 may be applied, unless otherwise provided for under international treaties executed by Mexico, except where there is no international reciprocity. Mexico has not executed any international treaties regarding liquidations or reorganisations or the like.

Chapter 12 aims to provide effective mechanisms for dealing with cases of cross-border insolvency with the following objectives: cooperation between Mexico and foreign courts; increase of legal certainty for trade and investment; fair and efficient administration of cross-border insolvency cases; protection and maximisation of a debtor’s assets; and facilitation of the rescue of financially troubled businesses, thereby protecting investments and preserving employment.

Chapter 12 applies where: assistance is sought in Mexico by a foreign court or a foreign representative in connection with foreign proceedings; assistance is sought in a foreign country in connection with a case under Mexican insolvency law; both foreign proceedings and a case under Mexican insolvency law with the same debtor are concurrently pending (parallel proceedings); or creditors, or other interested parties, in a foreign country want to commence or participate in a case under Mexican insolvency law.

Cooperation and communication between Mexican courts and foreign courts and between Mexican representatives and foreign representatives may be direct, without the need for letters rogatory or any other formalities.

#### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

The COMI of a debtor company is determined by the domicile it has registered in the commerce registry, where it has its main administration or main facilities and offices (headquarters).

In the case of corporate groups, when a petition has already been filed regarding a holding or subsidiary member of the same corporate group, the new petition shall be joint to the district court where the first was filed.

#### Cross-border cooperation

#### 49 Does your country’s system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

As stated above, the LCM incorporates generally the UNCITRAL Model Law. It provides for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings. It recognises court-to-court direct communication. Accordingly, direct cooperation is allowed between domestic courts and foreign courts as well as foreign insolvency administrators in cross-border insolvencies and restructurings. There have been instances between US and Mexican courts. Communications have been in writing in cases such as *Xacur*, *IFS* and *Satmex*.

Mexican courts under Chapter 12 of the LCM recognise foreign proceedings, such as those of *Xacur* and *IFS*.

Mexican courts have rejected recognition of a main foreign proceeding and to cooperate in cases whereby the debtor is not a merchant and therefore the UNCITRAL Model Law does not apply. In such a case, recognition of non-merchants, individuals or consumers shall be brought before state courts and state laws as insolvency proceedings for merchants.

**Cross-border insolvency protocols and joint court hearings****50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

In the *Xacur* and *IFS* cases Mexico had intensive court-to-court communication between the Mexican Fourth Federal District Court for Civil Matters, Honourable Judge Alejandro Villagomez Gordillo, and the US Bankruptcy Courts for the Southern District of Texas, Houston Division, Honourable Judges Karen K Brown and Marvin Isgur.

The *Xacur* case has established several precedents in Mexican jurisprudence regarding the UNCITRAL Model Law on Cross Border Insolvency, which is also applicable worldwide in foreign jurisdictions. The most significant of these precedents, which may be found in the *Semanario Judicial de la Federación*, are the following:

- Direct *amparo* 98/2003, Direct *amparo* 97/2003 and Direct *amparo* 96/2003 of 13 March 2003, regarding a foreign bankruptcy proceeding and the recognition and declaration of international cooperation. A judgment that recognises and grants international cooperation may be revoked.
- *Amparo in revisión* 282/2003, *amparo in revisión* 283/2003 and *amparo in revisión* 289/2003 of 5 September 2003, regarding a foreign

bankruptcy proceeding and the recognition and declaration of international cooperation. Indirect *amparo* may not be allowed against an order that decides a revocation remedy, derived from a decision entered in a judgment enforcement that recognises it, since it is not the last decision in this stage.

- *Amparo in revisión* 1588/2005 of 26 October 2005, regarding a commercial insolvency. Chapter 12 of the LCM is constitutional because it grants equal treatment to foreign and domestic creditors.
- *Amparo in revisión* 361/2004 of 27 October 2006, regarding the LCM. Standards for the recognition of foreign proceedings in Mexico.
- *Amparo in revisión* 361/2004 of 27 October 2006. International treaties only bind the states that are a party to the treaty.

These cross-border courts and their foreign representatives and professionals have created a legal vehicle in the form of general international cooperation by means of which they can communicate directly to immediately provide for recognition of foreign insolvency proceedings, protective measures, service of process, taking of all kinds of evidence abroad, sale of assets, criminal prosecution and the like. This vehicle harmonises the different legal systems of common law and civil law as well as domestic procedural law and practice. This vehicle has proved to be a very practical, efficient and effective tool, saving time and costs, making cross-border insolvency much more effective at optimising the activities and assets of the going concern for all involved.

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# Netherlands

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Dutch Bankruptcy Act currently provides for three different types of insolvency proceedings:

- bankruptcy, applying to companies, other legal entities and natural persons;
- (preliminary and definitive) 'suspension of payments', which can be granted to most companies and legal entities or to natural persons carrying out a profession or business; and
- debt reorganisation of natural persons.

A court may proclaim a debtor bankrupt when there is prima facie evidence that shows that the debtor has ceased to make payments. If a creditor petitions for the debtor's bankruptcy, the creditor also has to show prima facie evidence of his claim against the debtor. Pursuant to Dutch bankruptcy law, a debtor has ceased to make payments when the following criteria are satisfied:

- there have to be multiple creditors and at least one of the creditor's claims is due and payable; and
- the debtor has to have stopped making payments.

Suspension of payments does not apply to credit institutions and insurance companies. There are specific emergency regulations for credit institutions and insurance companies in the Netherlands Financial Supervision Act, which are based on Regulation (EU) 806/2014 (the Single Resolution Mechanism Regulation) (which amends Regulation (EU) 1093/2010) establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms, the Directive 2014/59/EU (the EU Bank Recovery and Resolution Directive) on the reorganisation and winding up of credit institutions and investment firms (which amends, among others, Directive 2001/24/EC), the Regulation (EU) No. 1024/2013 (the Single Supervisory Mechanism) on the policy of prudential supervision on credit institutions and the Directive 2001/17/EC on the reorganisation and winding up of insurance undertakings, respectively.

A legislative proposal regarding the pre-pack procedure is currently awaiting approval from the Dutch Senate and is expected to enter into force somewhere in 2017. See 'Update and Trends' for more information about the legislative proposal on the pre-pack.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The district court of the district where the debtor is or was last domiciled (for companies, this is the place of the statutory seat) has exclusive jurisdiction to open insolvency proceedings. If the debtor is not domiciled in the Netherlands, but has or had an establishment in the Netherlands, the district court of the district in which the establishment is or was located has exclusive authority to open the insolvency proceedings.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

#### Excluded entities

Dutch courts cannot open insolvency proceedings against a foreign state. Although the Dutch Bankruptcy Act does not contain exceptions, it is unlikely that insolvency proceedings could be opened against the Dutch state and local authorities, such as municipalities and provinces. For other Dutch governmental organisations this is less clear.

#### Excluded assets

There are a number of statutory exceptions that stipulate the exemption of certain assets to insolvency proceedings:

- assets that cannot be encumbered with attachments (in certain circumstances also copyright);
- the statutory exempt part of an individual's income;
- monies reserved for the bankrupted party derived from a statutory duty of support or maintenance;
- a supervisory judge may determine that property under administration is exempt from insolvency proceedings;
- monies that have been paid into court;
- assets under a regime of administration that have not been claimed by any creditor;
- based on case law, certain assets are exempt that are reserved from a prior bankruptcy;
- certain rights of use and the right of occupancy; and
- rights of a highly personal nature (such as for instance a right under an occupational pension scheme).

In certain situations it may prove difficult to determine whether an asset is excluded from insolvency proceedings. All relevant circumstances of each individual case may be relevant. Also in certain cases the cooperation of third parties may be important for instance in situations in which third parties will need to surrender their rights.

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

All entities in the sphere of private law can be declared bankrupt in accordance with the Dutch Bankruptcy Act. It is not certain if governmental bodies and administrative authorities of such entities can be declared bankrupt. However, the bankruptcy estate will not include assets that are destined for public service. Dutch law also provides for lower governmental bodies qualifying for supplemental support from the state, subject to those bodies relinquishing part of their financial policy autonomy to the state.

## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

#### Background

The Bank Recovery and Resolution Directive (BRRD) and the Single Resolution Mechanism (SRM) have created an EU legislative framework that deals with the failure of credit institutions and investment firms. The BRRD and the SRM are key components of the Banking Union's 'single rulebook' regulatory framework, which also applies in the Netherlands jurisdiction. The BRRD was implemented in the Netherlands in early 2016. For more detail on the BRRD and the SRM, see the European Union chapter.

The BRRD is a (minimum harmonising) EU directive and provides authorities with a common approach and a wide range of measures that can be taken to deal with failing credit institutions and investment firms. These measures can be divided over three phases: the preparatory and preventative; early intervention; and resolution.

The SRM is an EU regulation that is closely connected to the BRRD and creates a centralised resolution system for dealing with failing banks. The Regulation has direct effect and prevails over national law. The SRM confers special authority and powers to a new EU-level authority, the Single Resolution Board (SRB). Under the supervision of the SRB, each national resolution authority (in the Netherlands: the Dutch Central Bank) will be in charge of the execution of a resolution scheme.

#### Implementation in the Netherlands

The BRRD has been implemented in the Netherlands through the Dutch Implementation Act for the European Framework for the Recovery and Resolution of Banks and Investment Firms (the Recovery and Resolution Implementation Act), which entered into force on 1 January 2016. The Recovery and Resolution Implementation Act also purports to facilitate the application of the SRM. The Act, however, only covers areas of the BRRD that are not specifically provided for in the SRM (because of the direct applicability of the SRM). Therefore, both the SRM and the Recovery and Resolution Implementation Act need to be consulted to gain insight in the implementation and application of the new EU legislative framework within the Netherlands.

The SMR and the Recovery and Resolution Implementation Act both replace – for a large part – the Intervention Act, which was the previous legislative framework. The Intervention Act provided similar prevention, intervention and crisis management tools for distressed financial institutions that were deemed too big to fail (although the Intervention Act has largely been replaced by the new legislation, it is still relevant, see below).

Under the Recovery and Resolution Implementation Act, various amendments have been made to, among others, the Financial Supervision Act (FSA), the Civil Code and the Bankruptcy Act. A large part of the most significant changes can be found in the FSA, which introduces – among other things – a new Sub-Chapter (3A) entitled 'Special Measures and Provisions regarding Financial Undertakings'.

#### Recovery and resolution measures under the new legal framework

The Recovery and Resolution Implementation Act mirrors the same three-phase approach as set out in the BRRD (and SRM) – namely the preparatory and preventative phase, the early intervention phase and resolution phase. In conjunction with the SRM, the Recovery and Resolution Implementation Act provides specific rules and tools for each of those phases with respect to banks and investment firms (or groups containing such a bank or investment firm) that are based within the Netherlands.

With regard to the preparatory and preventative phase, there are new rules regarding recovery plans, intragroup financial support and resolution plans (which are prepared by the national resolution authority (ie, the Dutch Central Bank)).

With respect to the early intervention phase, new intervention tools are provided to the resolution authority, which aim to prevent the need for resolution of the bank or investment firm. Such early intervention tools include the supervisory authority instructing the relevant institution to implement a recovery plan, or to replace or remove members of its senior management or management body. Under certain

circumstances, it shall also be possible to appoint a temporary administrator, whose powers and authority shall be decided upon a case-by-case basis.

With regard to the resolution phase, the resolution authority is responsible for determining when and how a bank or investment firm becomes subject to resolution, provided that:

- the entity is failing or is likely to fail;
- there is no reasonable prospect that any alternative private sector measure or supervisory action would prevent the failure of that entity; and
- a resolution action is necessary in the public interest.

If these conditions are met, then the resolution authority may resolve to write down and convert capital instruments of the failing entity. If the resolution authority anticipates that the sole write-down and conversion of the capital instruments is insufficient to restore the financial soundness of the entity, then the resolution tools (individually or combined) may be applied: the sale of business or the bridge institution. For further information on each of these tools, see the European Union chapter.

The bail-in tool is a new provision under Dutch law, but the nationalisation of Dutch bank/insurer SNS Reaal (on 1 February 2013) effectively also involved a bail-in of subordinated debt of SNS Reaal and SNS Bank-issued debt instruments.

When a failing entity becomes subject to prevention or crisis management measures taken by the resolution authority, the Recovery and Resolution Implementation Act provides that under certain conditions the resolution authority is allowed to unilaterally terminate or amend contracts with third parties. Subject to certain requirements, the resolution authority may also decide to suspend payment or delivery obligations, or restrict or suspend the exercise of contractual termination rights (which also includes rights to accelerate, close-out, set-off or net) and security interests. These powers aim to enhance the effectiveness of the resolution tools. Note that some of these suspension powers are only applicable if the possibility for the counterparty to exercise their right is a result of a crisis prevention measure or crisis management measure, or any event directly linked to the application of such a measure. Furthermore, some suspension powers can only be applied temporarily. Finally, in some situations the use of these suspension powers is only allowed if the failing entity continues to meet the key obligations under the relevant contract, including the provision of collateral.

#### Safeguards to protect shareholders and creditors

The European Union legislative framework provides for several safeguards to protect the position of shareholders and creditors of a failed entity in the event that the resolution authority decides to use resolution tools. One of these is the 'no creditor worse off' principle. For further detail of these, see the European Union chapter.

Another safeguard entails the protection of counterparties in certain agreements (ie, security arrangements, financial collateral arrangements, set-off arrangements, netting arrangements, covered bonds and structured finance arrangements) who are confronted with the partial transfer of assets, rights and liabilities of a failed entity under resolution or in the event of forced contractual modifications (ie, amendment or termination). The Recovery and Resolution Implementation Act protects these counterparties by providing that the rights under those agreements may not be affected by such partial transfer. This means that if the resolution authority has decided to apply a partial transfer or if contractual modification takes place, then the resolution authority may not apply such partial transfer or contractual modification to certain agreements (such as set-off arrangements or financial collateral arrangements). Further, the resolution authority will also:

- not transfer an asset against which a liability is secured without also transferring the liability and the benefit of the security;
- not transfer a secured liability unless the benefit of the security is also transferred; or
- only transfer assets and liabilities jointly if they relate to a structured finance arrangement or covered bond.

#### The previous legal framework

While the new EU framework has led to significant legal changes in the Netherlands, the previous Dutch legislative framework that dealt with

distressed financial institutions (the Dutch Intervention Act, which entered into force on 13 June 2012), still has relevance. First, because the new EU framework only applies to banks (and investment firms). Therefore many provisions of the Dutch Intervention Act still apply to insurers, such as the authority of the Dutch Central Bank to, through a court order, transfer assets and liabilities of or shares in an insurer. Secondly, even though the new legislation has largely replaced the bank-related provisions in the Intervention Act, the special intervention powers that were granted to the Minister of Finance under the Intervention Act, remain in place (see Chapter 6 of the FSA). These powers include the power to transfer the deposits of banks, other assets and liabilities of a bank or insurer as well as the issued shares in the capital of a bank or insurer, and the power to expropriate assets or shares held in a bank or insurer.

Note that the Dutch legislator has stated that it considers these measures of the Intervention Act to be emergency legislation, which means that they are allowed to remain in place, despite the direct applicability of the SMR in the Netherlands. However, application of the SMR has priority over Dutch law. Therefore, the intervention powers granted to the Minister of Finance are seen as a 'last resort' and shall only be applied under extraordinary circumstances, which diminishes the importance of the 'old' intervention measures for banks under the Intervention Act.

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### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

Security over immoveable property (including leasehold) and certain registered moveables (registered ships and aircraft) is created by means of a right of mortgage. A right of mortgage is created by way of a notarial deed followed by registration in the relevant register (eg, the land register for real property).

The rights of the mortgagee are not affected by insolvency proceedings and the mortgagee is therefore able to act as if there were no insolvency proceedings, unless the court has granted a cooling-off period. A cooling-off period may be granted by the relevant court for up to two months, and can only be extended once, by a maximum of another two months. During the cooling-off period, the mortgagee cannot foreclose its security interests without court permission.

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### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

Security over moveable property is created by means of a right of pledge. There are two types of pledges over moveable property:

- a possessory pledge, where possession of the collateral is transferred from the pledgor to the pledgee or to a particular third party agreed upon by the pledgor and the pledgee; a possessory pledge does not require notarisation or registration; and
- a non-possessory pledge, where possession of the collateral remains with the pledgor. The deed of non-possessory pledge must either be drawn up in notarial form or registered with the tax authorities for the pledge to be valid.

Security over claims is also created by means of a right of pledge. There are two types of pledges over claims: a disclosed right of pledge and an undisclosed right of pledge, depending on whether the debtor of the claim has been given notice of the pledge. The disclosed pledge does not require notarisation or registration. The deed of the undisclosed right of pledge must either be drawn up in notarial form or registered with the tax authorities for the pledge to be valid.

The rights of a pledgee are not affected by insolvency proceedings and the pledgee is able to act as if there were no insolvency proceedings, unless the court has ordered a cooling-off period. This may be ordered by the relevant court for up to two months, and can only be extended once, by a maximum of two months. During the cooling-off period, a pledgee cannot foreclose its security interests without court permission.

In January 2006, Directive 2002/47/EC on financial collateral arrangements was implemented in the Dutch Civil Code, resulting in the introduction of the financial collateral arrangement, which is a security instrument for cash and financial instruments only between

certain categories of parties (in broad terms, 'financial institutions'). A financial collateral arrangement is created following an agreement between the parties and the execution of a pledge over the cash or financial instruments, or the transfer of the cash or financial instruments to the holder of the security that the financial collateral arrangement purports to create.

The rights of the holder of financial collateral are not affected by insolvency proceedings and it can act as if there were no insolvency proceedings, allowing the security holder to liquidate the assets over which it has security or, if agreed as part of the conditions of the security arrangement, retain ownership of the assets provided as security. Any cooling-off period ordered does not apply to assets subject to a financial collateral arrangement.

A supplier of goods may protect him or herself by inserting a retention-of-title clause in the supply contract. The clause will state that title to the goods supplied will not pass to the buyer until payment has been received. The seller cannot, however, reclaim the goods when these have been used in a manufacturing process such that accession occurred, nor does he or she have a right in the newly created goods. In addition, Dutch law provides for a statutory reclaim right for the seller of a moveable asset. The right to invoke this statutory right expires when six weeks have lapsed after payment was due and 60 days after delivery has taken place. The seller cannot exercise its statutory right to reclaim the goods when the goods have been used in a manufacturing process. During a cooling-off period, the supplier cannot effectively retake possession of the goods without court permission.

Furthermore, certain creditors holding the debtor's moveables or immoveables are able to invoke a right of retention, allowing them to withhold redelivery of the debtor's goods until receipt of payment of their claim. The creditor will obtain a preference over the proceeds of sale of the goods if a right of foreclosure is enforced against the goods, pursuant to a judgment granting authorisation to that effect.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

An unsecured creditor has to commence legal proceedings against the debtor for recovery of its debt if the debtor is unwilling to pay. Anticipating or pending such proceedings, the creditor may levy an attachment on assets of the debtor to ensure that the creditor can take recourse on assets of the debtor if a successful order is awarded. To levy such attachment, the creditor needs prior court approval, which can in general be obtained quite easily, and the attachment is levied by a bailiff, being a government-appointed person. If the outcome of the legal proceedings is successful, the creditor can foreclose on the attached assets and seize more assets if necessary.

The position of an unsecured creditor changes when insolvency proceedings are opened. Upon bankruptcy, unsecured ordinary and preferential creditors are no longer allowed to start or continue actions against the debtor to obtain payment of their claims, and any attachments that are levied are released by operation of law (save during a preliminary 'suspension of payments' when attachments will only be released when the preliminary 'suspension of payments' becomes definitive). Unsecured creditors must submit their claims to the bankruptcy trustee. Payment can only take place on a pro rata basis.

There are no special rules for foreign creditors except that, when a legal proceeding is pending, the court may in rare cases require a foreign creditor who initiated the legal proceeding to provide security for the debtor's legal costs, which are set by the court and rarely amount to more than several thousand euros.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Principally, a debtor can only implement a voluntary liquidation of its business in accordance with general corporate procedures if it is able to pay its debts or if it can agree a composition with its creditors. The relevant corporate procedure is liquidation by means of dissolution, whereby the shareholders' general meeting adopts a resolution to dissolve the company (see question 45).

The Bankruptcy Act also allows the debtor itself to request bankruptcy as a means to liquidate its assets. The directors of a company can only file for bankruptcy if the shareholders' general meeting instructed them to do so, unless the articles of association provide otherwise (see question 10).

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

##### Bankruptcy

A debtor can be declared bankrupt when it has ceased to pay its debts (see question 1). A creditor petitioning for a debtor's bankruptcy should therefore provide prima facie evidence that it has a claim against the debtor, the debtor has ceased paying its debts and there is at least one other creditor.

If the court declares the debtor bankrupt, the court will appoint at least one bankruptcy trustee and a supervisory judge. With retroactive effect from midnight as of the date of the bankruptcy judgment, the debtor is no longer authorised to manage and dispose of its assets. Only the bankruptcy trustee may do so. The trustee is charged with the administration and liquidation of the bankrupt estate. The trustee needs the approval of the supervisory judge for certain acts, including the disposal of assets, termination of employment agreements and initiation of legal proceedings.

During bankruptcy there is a general moratorium and ordinary and preferential creditors may no longer enforce their claims against the debtor's assets. Secured creditors are in general not affected by bankruptcy, except during a cooling-off period (see questions 6 and 7). In addition, there is the possibility for the bankruptcy trustee to set a time frame wherein the secured assets need to be sold by the mortgagee or pledgee. Failure to do so will result in loss of the right to foreclose on the assets (although their claims will continue to have a high preference, they will have to share in the costs of the bankruptcy).

##### Strike off

Apart from bankruptcy, the Dutch Civil Code also allows the relevant chamber of commerce or district court to dissolve a company if it has consistently failed to comply with certain statutory obligations.

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### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

##### Suspension of payments:

A 'suspension of payments' is the Dutch voluntary reorganisation proceeding for companies, legal entities and for natural persons conducting a business. The debtor can apply to the court for a 'suspension of payments' if it anticipates that it will be unable to pay its debts as they fall due. The directors of a company can request a 'suspension of payments' and they do not need the approval of the shareholders' general meeting, unless the articles of association provide otherwise.

Following the application, the court will grant a preliminary 'suspension of payments' and will appoint an administrator and also, in practice, a supervisory judge. The supervisory judge has a limited advisory role. The directors need the prior approval or cooperation of the administrator to enter into obligations that affect the assets of the company (see question 13). A 'suspension of payments' can be granted for a maximum of three years. It only has an effect on ordinary creditors, who are not allowed to enforce payment of their claims. Preferential and secured creditors are not affected, unless a cooling-off period has been granted (see questions 6 and 7).

Debtors can negotiate compositions with creditors outside insolvency proceedings. The disadvantage is that there are – except in rare situations – no opportunities to force a creditor to accept a general composition and that the composition is not court-supervised or approved.

##### Pre-pack procedure

In practice a process has been developed, which is used regularly and as part of which the debtor seeks the appointment of a bankruptcy trustee designate by the court in the period before the formal insolvency filing with a view to investigating restructuring options or to prepare for a formal filing, or both. The bankruptcy trustee designate is appointed

by the court prior to the commencement of a formal insolvency procedure. The debtor and its stakeholders (creditors, including lenders) act on the assumption that the bankruptcy trustee designate is to be appointed by the court as the insolvency office holder once a formal insolvency procedure is opened. The pre-pack procedure has now been codified in a legislative proposal, the Continuity of Companies Act I, which is currently being reviewed by the Senate. See 'Update and trends' for more information about the legislative proposal on the pre-pack.

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### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Creditors cannot force or direct a reorganisation. However, if a bankruptcy petition is presented against the debtor it can counter with a request for a 'suspension of payments' by the debtor, often with the aim of avoiding bankruptcy for as long as possible. By law, a petition for a 'suspension of payments' is dealt with before a petition for bankruptcy.

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

There is no specific statutory obligation for managing directors to file for bankruptcy or seek a suspension of payments. However, in certain circumstances, managing directors or shareholders may be personally liable in tort towards creditors of the company if they decided to continue the business past a certain point in time (and that decision resulted in damage to the creditors). Other than under certain circumstances personal liability for the directors, there are no consequences if a company carries on business while insolvent, save for a Dutch public limited liability company which is obligated to call a shareholders meeting if it has negative equity.

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

##### Reorganisation outside insolvency

If the reorganisation takes place outside the scope of formal insolvency proceedings, the normal rules of representation will remain effective. This would apply to the pre-pack procedure as well. During the pre-pack phase the debtor remains authorised to manage and dispose of its assets.

##### Reorganisation within 'suspension of payments'

If the reorganisation occurs in the context of a 'suspension of payments', the managing directors need the prior approval or cooperation of the administrator to enter into obligations that affect the assets of the company. If a bankruptcy trustee continues a contract with a supplier in a 'suspension of payments', the supplier may request a bankruptcy trustee to provide security for the obligations of the debtor, which the bankruptcy trustee must then do.

##### Bankruptcy

Upon bankruptcy, only the court-appointed bankruptcy trustee is entitled to dispose of the assets of the debtor. The trustee needs the approval of the supervisory judge for certain acts, including continuation of the business of the debtor and a sale of assets. If a bankruptcy trustee continues a contract with a supplier after bankruptcy, the bankruptcy trustee is obliged to provide security in respect of the obligations of the debtor. The corporate law capacities of the directors remain unaltered (for example capacity to convene a shareholders meeting, to

appoint directors, to deposit accounts with the trade register), however the directors no longer have the power to bind the company.

The Bankruptcy Act allows for the appointment of a creditors' committee by the supervisory judge to advance the interests of the creditors that has certain powers to supervise and advise on the settling of the estate by the bankruptcy trustee. Such a creditors' committee can be appointed if the importance or nature of the estate provides a cause to do so. The task of the creditor's committee is to give advice and exercise (if necessary) any of the specific powers given to it (for example, to file an objection against any act of the bankruptcy trustee with the supervisory judge). The reason for having such a creditors' committee is to allow a greater degree of involvement by the creditors. However, in practice, creditors' committees are rarely appointed.

#### Stays of proceedings and moratoria

- 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

##### Bankruptcy

As a result of the bankruptcy order, there is an automatic stay, and legal proceedings that require the performance of an obligation by the debtor are suspended. Only a limited number of legal proceedings, for example, where a supplier claims or reclaims ownership, are not affected by the bankruptcy judgment and these can be continued. Secured creditors are not affected by the stay, unless a cooling-off period is ordered by the court (see questions 6 and 7).

##### 'Suspension of payments'

In a 'suspension of payments', there is only a limited stay unless a cooling-off period is ordered by the court (see questions 6 and 7). Preferential and secured creditors are, in the absence of a cooling-off period, not affected by the suspension of payments. Even unsecured ordinary creditors can initiate or continue legal proceedings, although they cannot foreclose a judgment against the assets of the debtor to enforce payment.

#### Post-filing credit

- 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

##### Bankruptcy

The bankruptcy trustee can obtain loans or credit. The obligations arising as a result of these loans or credit extended to the trustee in bankruptcy are considered to be estate claims and they have a high ranking. Security can be granted over assets to secure repayment.

##### 'Suspension of payments'

The managing directors can, with the consent of the administrator, obtain loans or credit. Credit granted during a 'suspension of payments' does not automatically have a high ranking, but in practice will often be fully secured.

#### Set-off and netting

- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

Prior to bankruptcy a creditor can set off a claim if the following requirements have been met: mutual indebtedness, the performance of the obligation corresponds to the claim, the creditor is entitled to perform its obligations (pay its debts) and the creditor's claim is due and payable. The creditor should give notice of the fact that he or she sets off the claims against the debtor and debts to the debtor. Parties may make different arrangements.

During a 'suspension of payments' or bankruptcy, the right of set-off is broader. The creditor may set off claims and debts if both the claim and the debt existed prior to the opening of the insolvency proceedings or the opening of a 'suspension of payments' or resulted from acts that were performed prior to the opening of the insolvency proceedings

or 'suspension of payments' respectively. The requirements that the creditor must be entitled to perform its obligations (to pay its debts) and that the claim against the debtor must be due and payable do not apply. A creditor, however, is not allowed to set off claims if it obtained the debt or the claim against the debtor at a time that it knew or should have known that the debtor would go bankrupt or would file for a suspension of payments.

#### Sale of assets

- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

##### 'Suspension of payments'

In a 'suspension of payments' only the directors and the court-appointed administrator acting jointly will be able to bind the company and dispose of assets of the company (see question 14). There is no distinction between the sale of goods within or outside the ordinary course of business; therefore, claims may in certain cases pass with the assets.

##### Bankruptcy

Upon bankruptcy, only the court-appointed bankruptcy trustee can dispose of the debtor's assets. The sale of assets can take place by way of a public sale or a private sale. The bankruptcy trustee needs the approval of the supervisory judge for a private sale of assets. Often, depending on the method of sale chosen by the bankruptcy trustee, assets can be transferred free and clear, for instance, when a bankruptcy trustee sells real estate or assets for the benefit of a mortgagee or pledgee; however in other circumstances, third-party rights may pass with the assets, for example, rights of a tenant leasing a property which is sold.

Based on case law from lower Dutch courts, the bankruptcy trustee is obliged to investigate carefully the value of the assets in order to obtain the highest proceeds for such assets, meaning that he or she should look for alternative bidders should the received bids not be reasonable. The bankruptcy trustee may be liable when he or she intentionally prejudiced the creditors in any way. Although not specifically referred to in the Bankruptcy Act, credit bidding in sale procedures is not unknown in the Netherlands.

Holders of security rights over assets in a bankruptcy estate are able to exercise their rights as if no formal insolvency procedure has occurred. They are able to proceed to an enforcement sale of the assets in accordance with the statutory rules regarding enforcement sales. An enforcement sale can take place by way of a public sale (auction) or private foreclosure sale. An appropriation of the assets by the security holder is prohibited. However, the holder of the security right is allowed to participate in the auction process as a bidder. In case of an enforcement sale in respect of real estate there is a statutory requirement for the payment of the proceeds in cash to the notary that runs the enforcement process, which limits the ability to credit bid. This, however, does not mean that economically a credit bid cannot be achieved through, for instance, a daylight facility. The requirement that proceeds must be paid in cash to a notary or bailiff does not apply in the case of an enforcement sale of pledged assets. This means that in some instances there may be the possibility to implement a credit bid.

#### Intellectual property assets in insolvencies

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

##### Insolvency of a licensor

The position of an IP licence after insolvency has been subject of fierce debate in both academic circles and within the Dutch courts. In a judgment in 2006 (the *Nebula* judgment), the Supreme Court ruled that the

principle that reciprocal agreements continue during insolvency does not mean that the creditor of such an agreement is free to continue exercising his rights under the agreement as if there is no insolvency. The Supreme Court decided that the principle of equality of creditors outweighs the continuation of reciprocal agreements after insolvency. Therefore, the creditor was not permitted to invoice the right of use of a licence after the insolvency. Notwithstanding that this specific case concerned tenancy rights the Attorney-General introduced a parallel with IP rights.

The Supreme Court's decision in the *Nebula* judgment was generally interpreted (both in legal literature, as well as in legal practice) as a right of the bankruptcy trustee to actively breach a reciprocal agreement. However, it appears that the Supreme Court has overturned the *Nebula* judgment in 2014 in its *Berzona* judgment, and that the right of a bankruptcy trustee to actively breach a reciprocal agreement does not extend to certain types of agreements. From the 2014 *Berzona* judgment it follows that a distinction can be made between reciprocal agreements in which:

- performance of the agreement by the bankrupt debtor requires a certain act from the bankruptcy trustee (at the expense of the estate), such as a payment or the delivery of goods; and
- performance of the agreement by the bankrupt debtor (solely) requires the bankruptcy trustee to honour the creditor's contractual right of use (eg, a lease agreement).

With respect to the second type of reciprocal agreement, the Supreme Court held that the bankruptcy trustee does not have a right to breach such agreements and that the bankruptcy trustee must honour the creditor's right of use. The *Berzona* judgment concerned the rights of use of a tenant vis-à-vis the right of the bankruptcy trustee to breach the lease. As was the case with the *Nebula* judgment, the Supreme Court's decision appears to be also relevant for other types of reciprocal agreements, such as licensing agreements. In practice this would mean that in the event a licensor is declared bankrupt, the bankruptcy trustee must respect the licensee's right of use (in principle for as long as the licensing agreement is in place).

### Insolvency of a licensee

The position is different as regards the insolvency of a licensee because any reciprocal agreements should continue during insolvency an insolvency administrator should be able to continue to exercise the IP rights granted under the licence. This means that unless provided otherwise in the licence, the opening of insolvency proceedings in respect of the licensee does not impact the rights of the licensor. If the licensee becomes insolvent and the licensee has fully performed its obligations under the licence, the licensee's insolvency administrator is entitled to claim performance of the licensor. Furthermore, the insolvency administrator may also seek to terminate the licence.

To the extent that the licensor has fully performed its obligations under the licence and has a claim against the insolvent licensee, the licensor may seek termination of the licence on the basis of the general provisions of breach of contract, unless the insolvency administrator performs the licence. The licensor's claim resulting from termination of the licence will be unsecured.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Personal Data Protection Act, which entered into force on 1 September 2001, provides mandatory rules on the protection, processing and storing of personal data. Any party that is processing personal data (for instance, by collecting personal information), must comply with the Personal Data Protection Act. Personal data can be any information related to a natural person (such as employees or customers of a company).

Personal data may only be processed when:

- the person involved has unambiguously granted consent;
- it is necessary in relation to an agreement to which the involved person is a party or shall become a party;
- it is necessary because of a statutory obligation;

- it is necessary to protect the health of the person involved;
- it is necessary for the proper performance of a public-law obligation; or
- when it is necessary to protect a legitimate interest of the processor or a third party that receives the personal data, unless such interest violates the fundamental rights of the person involved (eg, the right to privacy)).

Furthermore, the Personal Data Protection Act prohibits processing or further use of the personal data when:

- this is incompatible with the purposes for which the data were acquired; or
- an official, professional or statutory duty of confidentiality stands in the way of processing the personal data.

Once personal data have been processed (eg, collected, gathered, stored, categorised or used in any other way) in accordance with the Personal Data Protection Act, they must be adequately protected against loss or any form of illegal processing. If a company has processed personal data and goes insolvent, it must still adhere to the Personal Data Protection Act. The mandatory rules of the Personal Data Protection Act also apply when (processed) personal data are transferred to another party. Transfer of personal data to a third party is not explicitly prohibited in the Personal Data Protection Act, but the transferee must comply with the mandatory rules regarding the processing of personal data and the (further) use of personal data.

In practice, this means that when a bankruptcy trustee decides to sell personal data held by the insolvent company to a third party, the bankruptcy trustee or the buyer, or both, actively seek out the consent of the persons involved by informing them of the intended transfer and the intended use of the personal data. When informing the persons involved, the bankruptcy trustee or buyer, or both, usually offer them the opportunity to object against the processing of their personal data by the buyer (ie, an opt-out). If a person opts out, then his or her personal data will be excluded from the envisaged transfer. This is a practical way for the bankruptcy trustee and the buyer to ensure that they act in accordance with the Personal Data Protection Act.

### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

Yes. As a general rule, Dutch law provides that contracts continue after insolvency of a counterparty, unless the contract includes an ipso facto (or insolvency) clause (pursuant to which the contract automatically terminates (or may be terminated) on insolvency).

The Bankruptcy Act, however, allows the bankruptcy trustee to confirm or terminate executory contracts under which both the debtor and its counterparty have outstanding obligations (where he or she believes that continuation of the contract is not in the best interest of the debtor's creditors as a whole). Any creditor can request the bankruptcy trustee to confirm within a reasonable time whether a contract will be honoured by the estate. If the bankruptcy trustee does not provide such confirmation the estate forfeits the rights to request performance of the contract. The contract is considered terminated and the counterparty has an unsecured and non-preferred claim for damages. If the bankruptcy trustee decides to confirm continuation of the contract, the estate must provide security for the proper performance of its obligations, for example a right of pledge, mortgage or personal right (such as surety or a liability statement). The security should be sufficient to cover the claim and if applicable, any related interest and costs, in such a manner that a creditor can effortlessly take recourse. Security may include bank guarantees or the creation of security over unencumbered assets. Typically, a negative pledge undertaking in the finance documentation does not create a limitation. Only to the extent that actual security has been created, for the benefit of the financing bank over the assets does this create a limitation. After the provision of security, the contract will then have to be performed by both parties. If the bankruptcy trustee breaches such a contract, the creditor will be able to enforce its security rights.

For contracts where the estate is not under an obligation to actively perform but is only required to omit or tolerate a different regime applies. For these contracts, such as lease contracts or IP licences, the bankruptcy trustee may not simply reject the contract or terminate it, save as specially provided for in the Bankruptcy Act. This has been confirmed in case law of the Dutch Supreme Court (see question 19). The Bankruptcy Act contains specific provisions for the termination of certain types of contracts, such as leases and employment contracts. To terminate those types of contracts the bankruptcy trustee has to take into account fixed notice of terms as set out in the Bankruptcy Act.

As a final note, it is of course also possible that a creditor wishes to terminate a contract because of the debtor's insolvency. As stated above, if the contract includes an insolvency clause, then the creditor may exercise the termination rights arising from such a clause, as agreed under the contract. However, pursuant to case law of the Dutch Supreme Court (the *Megapool/Laser* judgment) there are exceptions to this general rule.

In *Megapool/Laser* the Dutch Supreme Court identifies two possible scenarios in which an insolvency clause may be null and void (subject to the context and other circumstances of the case at hand):

- if (solely) because of the occurrence of the debtor's insolvency the creditor's obligation to perform under the contract no longer applies, where the debtor has already performed its obligation, the insolvency clause may be considered to infringe on the central principle of Dutch bankruptcy law that the legal position of creditors is fixed as of the commencement of the bankruptcy; or
- if exercise of the insolvency clause is contrary to the overriding principle of reasonableness and fairness.

Permitting the exercise of insolvency clauses under those circumstances would disproportionately prejudice the other creditors' recourse options, because an asset of the debtor (ie, its rights under the contract) are being kept out of the estate of the bankrupt debtor solely because of its bankruptcy.

#### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Parties, including the bankruptcy trustee may choose to submit disputes to arbitration. The courts in the Netherlands, however, do not have the power to direct the bankruptcy trustee or its counterparty to submit disputes in the bankruptcy procedure to arbitration. There are certain types of insolvency disputes that may not be arbitrated, for example disputes regarding matters of public concern. A distinction should be made between arbitration procedures pending at the time of the commencement of the bankruptcy case and procedures commenced afterwards to solve a dispute related to the insolvency.

#### Pending arbitration

Arbitration proceedings regarding monetary claims or for breach of contract that are already pending at the time the insolvency proceedings are commenced are suspended through analogous application of the statutory provisions in the Bankruptcy Act dealing with litigation in a governmental court. If the claim is contested by the bankruptcy trustee, the arbitration may be continued to determine the amount of the creditor's claim that will be admitted for proof.

#### Post-insolvency disputes

Arbitration procedures do not typically play a substantial role in the insolvency process, although the bankruptcy trustee in principle is authorised to agree to arbitration on behalf of the estate (ie, claims by the estate are arbitrable). Claims against the debtor that do not involve the estate (ie, which are not aimed at retrieving payment from the estate) may also be submitted to arbitration. Neither the Bankruptcy Act nor case law directly addresses whether a contested claim for payment in the claims allowance stage, in respect of which no arbitral proceedings were pending when the insolvency proceedings were

commenced, is arbitrable. There are differing views in legal literature, and the wording of the relevant provision of the Bankruptcy Act seems to preclude arbitrability. There is, however, a case of the Dutch Supreme Court in which the court found that a choice of forum for a foreign court was binding upon a bankruptcy trustee where he seems to reject or challenge a claim. It is not unlikely that the courts will come to the same conclusion with respect to an arbitration clause and require the bankruptcy trustee to arbitrate the claim.

#### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

##### Outside insolvency

A reorganisation outside of insolvency will only be binding upon those creditors that agree to the plan. Only in very specific situations, where it would be wrongful not to vote in favour of the plan, for example, if the creditor in all reasonableness should not have refused to cooperate as it abuses its position in doing so, is it possible to force a creditor to accept the plan by a court order to that effect. To date the Dutch High Court has rejected many attempts to claim such an abuse of position.

##### Within insolvency

A reorganisation plan may be proposed by the debtor in a bankruptcy or in a 'suspension of payments'.

There are no mandatory features of a reorganisation plan except that it should take into account the statutory grounds for rejection (see below). A successful reorganisation, however, often relies upon preparation and securing the cooperation and commitment of major creditors to it before filing for a suspension of payments.

A plan that is accepted by a majority of creditors, as set out below, and approved by the court will be binding on all unsecured creditors (regardless of whether or not they submitted their claims and whether or not they voted in favour of or against the plan). Preferential and secured creditors are not bound by the plan, unless they so agree. Unsecured creditors that submitted their claims (which were accepted or conditionally admitted) and are present at the meeting of creditors must approve the plan by a simple majority representing at least 50 per cent of the total value of the unsecured claims against the debtor. If the required majority do not vote in favour of the plan, the supervisory judge may, upon request, nevertheless approve the plan if at least 75 per cent of those creditors who submitted their claims (which were accepted or conditionally admitted) approved the plan, provided that the rejection of the plan is because of one or more creditors who could not reasonably have been expected to vote against the plan.

The court will not approve the plan (even if the thresholds referred to above have voted in favour of the plan) if:

- the value of the assets in the estate is significantly higher than the amount offered to the creditors;
- the performance of the plan is not sufficiently guaranteed;
- the plan has been accepted as a result of fraud, preferential treatment of certain creditors or as a result of other unfair methods; or
- there are any other grounds why the court believes that the plan should not be approved.

Acceptance of a reorganisation plan does not automatically result in a release in favour of third parties. Any type of release in favour of third parties will need to be specifically negotiated and agreed.

#### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

Officially, there is no special provision for expedited reorganisations. However, in practice, bankruptcies are regularly pre-packaged in the sense that sale of the business to a newly incorporated entity is organised. A pre-pack takes place through the appointment of a *beoogd curator* (bankruptcy trustee designate), which is appointed by the court at the request of the business. The court will test whether the appointment of a bankruptcy trustee designate is justifiable. See 'Update and trends' for more information about the legislative proposal on the pre-pack.

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## Unsuccessful reorganisations

### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

#### Outside of insolvency

A dissenting creditor can decide not to take part in a reorganisation that takes place outside of insolvency. Save for exceptional situations, he or she will not be bound by any plan agreed with other creditors. In the case of a pre-pack, the debtor's creditors, the bankruptcy trustee designate or the intended supervisory judge are each entitled to request the court to terminate the pre-pack procedure. See the 'Update and trends' for more information about the legislative proposal on the pre-pack.

#### Within insolvency

A reorganisation plan in insolvency proceedings is defeated if the majority of creditors does not approve the plan or the court does not approve the plan. In the case of a suspension of payments, the court must terminate the suspension of payments and declare the debtor bankrupt (see question 23).

If the debtor does not perform the plan after it has been approved by the court, the plan can be dissolved and the court will open or reopen the bankruptcy proceedings.

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## Insolvency processes

### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The opening and termination of insolvency proceedings are published in the government gazette and in the national insolvency register. This is an electronic register accessible online, in which all bankruptcies, suspensions of payment and debt reorganisations of natural persons opened after 1 January 2005 have been registered. Typically, it takes from one to several days between a company being declared bankrupt or 'suspension of payments' being ordered and publication in the register. To determine whether a company was declared bankrupt before 1 January 2005, it is still necessary to contact the relevant courts to confirm that the register is up to date. In addition, there is a separate register, kept by the court in The Hague, in which foreign insolvency proceedings that have been recognised under the EU Insolvency Regulation can be registered at the request of a foreign administrator.

If a creditors' meeting is held, this will also be made public in one or more newspapers. The bankruptcy trustee will also separately notify all creditors in writing of a creditors' meeting. A creditors' meeting is held if there are sufficient assets to make distributions to the unsecured creditors. During a creditors' meeting, all claims of creditors are verified and listed. Claims can either be admitted or challenged (see question 31).

If it is likely that there will be insufficient assets to distribute to the unsecured creditors, the bankruptcy judge may decide – at the request of the bankruptcy trustee – that it will not be necessary to deal with the unsecured claims and that there will not be a meeting at which claims are admitted or rejected. The bankruptcy trustee will then notify all creditors of this decision in writing and he or she will also announce the decision in one or more newspapers. Once the bankruptcy trustee has prepared a distribution plan for the estate and preferential creditors (see question 33), this will be filed with the court for inspection by the creditors. The filing will be announced in one or more newspapers and to the known creditors by separate letter.

In addition, a creditors' meeting is held in a 'suspension of payments' to vote as to whether the provisional 'suspension of payments' should be converted into a definite 'suspension of payments' to vote on an extension of the definite 'suspension of payments' or to vote on the acceptance of a reorganisation plan (see question 23).

At the end of each three-month period, the bankruptcy trustee must report on the state of affairs of the estate. The bankruptcy trustee must deposit his or her report with the clerk's office at the district court, where it will be available for public inspection free of charge. The three-month period may be extended by the supervisory judge.

As a general rule, the ability to bring proceedings against third parties in relation to losses suffered by the company is confined to the bankruptcy trustee. However, creditors may, in certain circumstances, pursue remedies against third parties, including directors and shareholders on the basis of tort (see question 41). Such procedures may be suspended by the court where they are brought until a decision has been reached in the procedure initiated by the bankruptcy trustee.

Currently the debtor is unable to effect a compulsory composition between the debtor and the third party creditors outside formal insolvency proceedings. See 'Update and trends' for more information about the pending legislative proposal on the compulsory composition for release of liability by guarantors.

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## Enforcement of estate's rights

### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Under certain circumstances, a bankruptcy trustee may apply to the Ministry of Security and Justice to obtain financing to pursue claims against the directors and supervisory board directors. Any proceeds will be available for distribution to the creditors.

Alternatively, a bankruptcy trustee may seek to assign a claim to obtain financing to pursue other claims. Note, however, that the bankruptcy trustee cannot assign his own claim based on the statutory anti-abuse provisions.

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## Creditor representation

### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The Bankruptcy Act allows for the appointment of a creditors' committee by the supervisory judge (see question 14). The creditors' committee may demand inspection of the books, records and other data carriers relating to the bankruptcy at any time. The bankruptcy trustee must provide the creditors' committee with such information as the committee requires.

The bankruptcy trustee must obtain the advice of the committee on several instances such as whether to continue the business of the debtor and in respect of the manner of the liquidation and realisation of the estate and the time and amount of the distributions to be made. The bankruptcy trustee is, however, not bound to accept the advice of the committee.

There are no specific provisions that deal with retaining advisers or the funding of expenses.

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## Insolvency of corporate groups

### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

The Bankruptcy Act does not recognise the concept of consolidated reorganisation. In practice, a bankruptcy trustee or administrator appointed at the parent level may seek appointment at the subsidiary level also and realise a de facto combined administration for administrative purposes. However, from a legal point of view, each proceeding remains distinct and separate from the other, as are the creditors of the various entities. In the event of possible conflicts of interest between the (creditors of the) various entities belonging to a group of companies, the court may appoint different individuals as bankruptcy trustees or administrators of the entities involved, who then among them – with the approval of the court – may attempt to come to an arrangement that takes into consideration that the various companies prior to opening of the insolvency proceedings used to operate as a group, that is, as one economic entity.

A distinction should be made between countries to which the EU Insolvency Regulation applies and other non-EU jurisdictions (including Denmark). The transfer of assets is allowed with respect to member states where the EU Insolvency Regulation applies.

When only a main proceeding is opened all of the debtor's assets are subject to the main procedure. The liquidator may exercise all the powers conferred on him by the law of the state of the main proceeding in another member state, as long as no secondary proceedings have been opened. The office holder may remove the debtor's assets from the territory of the member state in which they are situated.

Also pursuant to the EU Insolvency Regulation the administrator of the secondary proceeding shall need to give the office holder of the main proceeding the right to use the assets of the secondary proceeding. This becomes relevant when the office holder in the main proceeding would like to restructure the business and sell it as a whole, including the assets involved in the secondary proceeding.

With respect to insolvency proceedings opened in countries which do not belong to the EU and where the EU Insolvency Regulation does not apply, Dutch bankruptcy law, although it recognises the authorities of a foreign insolvency officer under the *lex concursus*, does not recognise the effects of the foreign insolvency to such an extent that creditors are prevented from taking recourse on assets located in the Netherlands belonging to the debtor to which the foreign insolvency procedure applies. In Dutch case law, however, it is determined that a foreign insolvency office holder is allowed to invoke its rights in the same way as is available to the foreign insolvency office holder under domestic insolvency law, including over assets which are located in the Netherlands. The office holder is also allowed to sell these assets and consider the proceeds part of the assets of the foreign bankruptcy estate. Notwithstanding that the foreign insolvency procedure's seizure is regarded as having only territorial effects of the foreign insolvency, the effects are *de facto* recognised in the Netherlands. In the EC Regulation on Insolvency Proceedings 2000 (Council Regulation (EC) No. 1346/2000) (the Recast Regulation) a new mechanism is introduced for a group coordination plan. This regulation is in force at the time of writing although the majority of its provisions will only apply from 26 June 2017. Insolvency proceedings opened after 26 June 2017 in member states (other than Denmark) will fall under the scope of the Recast Regulation. An officeholder appointed in any insolvency proceeding will be able to request the opening of group coordination proceedings where more than one member of a group is in insolvency proceedings. The court first seized will have jurisdiction to consider the request. For further detail on the Recast Regulation and the timings of its effect please refer to the chapter on the European Union.

## Appeals

### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Under Dutch bankruptcy law, a debtor, a creditor, the Public Prosecution Service, or any other interested party are each granted rights to appeal (or oppose) a decision on a bankruptcy request. These rights arise automatically. Permission to appeal (or oppose) a decision on a bankruptcy request is not required. The various rights of appeal (or opposition) can be summarised in the following scenarios.

#### Rights of appeal when the court rejects a bankruptcy request

If a bankruptcy application is rejected by the court, then the applicant (either a debtor who applied for his or her own bankruptcy, a creditor, or the Public Prosecution Service) are each entitled to lodge an appeal against that decision with the court of appeal within eight days of the date of the rejection (note that this appeal option is not open to a creditor that did not file for the debtor's bankruptcy).

#### Rights of appeal and opposition when the court grants a bankruptcy request

The debtor who was declared bankrupt at the request of a creditor or the Public Prosecution Service can appeal against this decision with the court of appeal, within eight days of the day of the bankruptcy declaration.

If the debtor has not been heard by the court prior to the bankruptcy declaration, he has 14 days after the day of the bankruptcy declaration to oppose that decision at the court that decided on the bankruptcy application (note that this does not apply if a debtor filed for his or her

own bankruptcy). The 14-day term can be extended to a month if it concerns a debtor who – at the time of the bankruptcy declaration – was not located within the borders of the Netherlands. If the court upholds the bankruptcy declaration in these opposition proceedings, then the debtor may lodge an appeal against that judgment with the court of appeal, within eight days of the day of the court's decision on the opposition.

A creditor that did not file for the debtor's bankruptcy or any other interested party also has the right to oppose a bankruptcy declaration. For such parties the opposition term expires eight days after the day of the bankruptcy declaration. If the court upholds the bankruptcy declaration in these opposition proceedings, then the creditor or interested party may lodge an appeal against that judgment with the court of appeal, within eight days of the day of the court's decision on the opposition.

#### Rights of appeal when an opposition against a bankruptcy declaration is successful

If the opposition by a creditor or interested party is granted and subsequently the initial decision to declare the debtor bankrupt is annulled, then the debtor, the creditor who filed the bankruptcy request, or the Public Prosecution Service have the right to appeal against that decision within eight days.

If any of the appeal/opposition scenarios set out above lead to a decision by the court of appeal, then that decision can also be appealed against by anyone who was a party to the appeal procedure. Such an appeal must be lodged with the Supreme Court, within eight days of the day of the decision by the court of appeal.

There is no statutory requirement to post security when bringing an appeal before a Dutch court. A defendant can request the court to order the claimant to post security for payment of the litigation costs (usually by way of a bank guarantee), but only if the claimant does not live (or has an office) in the Netherlands. However, there are numerous exceptions to this rule. For instance, if the claimant is from a country in which the EU Execution Regulation or the Civil Procedure Convention 1954 is applicable, then such request cannot be made. Also, under certain circumstances ordering a party to post security can be a violation of the 'equality of arms principle'. Owing to the various exceptions, the practical use of the possibility for a defendant to request the court to order the claimant to post security is limited.

## Claims

### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Claims must, as a rule, be submitted to the bankruptcy trustee 14 days prior to the meeting at which creditors' claims are accepted or rejected (the 'claims allowance meeting') (for foreign creditors, a limited exception is possible). During a 'suspension of payments' a similar procedure applies, albeit a claim is only admitted with the aim to vote on the reorganisation plan submitted by the debtor. As a result, there is, unlike in a bankruptcy proceeding, no formal procedure available to litigate a claim if it is disputed. The bankruptcy trustee will decide whether he or she will admit or challenge a claim. Other creditors may also challenge the admittance of a claim. If he or she admits a claim, the claim is placed on a list with provisionally admitted claims. If the bankruptcy trustee challenges a claim, that claim will be placed on a separate list. During the claims allowance meeting, all claims are reviewed and when claims are challenged and no solution can be reached, the supervisory judge will refer the matter to legal proceedings on the merits, in which case the validity of the claim will be litigated.

There are no specific provisions that deal with the purchase, sale or transfer of claims against the debtor.

It is possible that claims that represent an unliquidated amount are recognised in a bankruptcy proceeding. The Bankruptcy Act determines that claims that do not reflect the amount in euros or claims that are indefinite, uncertain or not expressed in money must be verified for their estimated value (in euros). The estimation should be based on the value on the day that the company was declared bankrupt.

If the estimation of the value of a claim is not possible, but there is a likelihood that the value can be determined at a later stage, the allowance of the claim takes place on a preliminary basis. Such claim can be added as *pro memorie* to the list of known or disputed creditors.

The Bankruptcy Act provides also for the allowance of claims with an uncertain due date or claims that entitle the claimant to periodic payments. In such a case, the claim will be admitted for its value at the date of the bankruptcy order. Claims that become payable within a year of the commencement of the bankruptcy will be considered due as of the date of bankruptcy. Claims that become payable after one year will be admitted for their value one year from the date of the commencement of the bankruptcy. For calculation only, the intervals of instalment payments, any profit opportunity and, if the claim bears interest, the agreed rate of the interest will be taken into account. In principle, to the extent secured by in rem security rights, a claim acquired at a discount secured by security can be enforced for its full value. However, there are limitations on the acquisition of claims with a view to setting off claims at a point in time bankruptcy becomes unavoidable or with a view to bringing the claim under the scope of foreign security rights. Interest accrued after the opening of an insolvency case cannot be claimed by a creditor.

### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

No. Dutch law does not recognise a concept similar to 'priming'.

### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

A bankruptcy trustee will first pay estate claims and thereafter the pre-insolvency claims. Estate claims generally are claims incurred by the bankruptcy trustee in performing his duties, and that fall in the estate without requiring verification, which just like insolvency costs have priority above the ordinary and preferred debt claims against the debtor. Estate claims are deemed to include debts which give an immediate claim on the estate, because they are claims arising out of contracts continued or made by the bankruptcy trustee. With respect to the pre-insolvency claims, a distinction should be made between preferential claims (the majority of which tend to be held by the tax authorities and social security board) and unsecured claims. Preferential claims can again be subdivided between claims that have a general preference and claims that are preferential only in relation to a specific asset. Furthermore, the rank of preference may vary.

Claims that have a general preference include:

- claims for the costs of the filing of bankruptcy; and
- taxes and social security premiums.

Claims that are preferential in relation to a specific asset include:

- claims in connection with the preservation of an asset;
- claims secured by a right of mortgage or right of pledge; and
- claims in connection with a right of possession.

### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

The strict requirements that apply to the dismissal of employees outside bankruptcy do not apply in the case of bankruptcy. This means that, in practice, bankruptcies are regularly used for restructuring purposes.

An employee may have two claims with different priority. A distinction should be made between the period before the bankruptcy (pre-insolvency) and after the opening of the bankruptcy. The unpaid salary, pensions and other related benefits deriving from the employment contract that fell due before the bankruptcy are preferential claims with a general preference (see question 33). From the day the company is declared bankrupt salary, pensions and other related benefits deriving from the employment contract are an estate claim.

In addition to the above-mentioned claims of employees, a wage guarantee by the Dutch Employee Insurance Agency (UWV) exists in

the Netherlands. When the employer is unable to pay the salary of the employee, the UWV will guarantee the salary for up to 13 weeks before the termination of the employee's employment contract by the bankruptcy trustee. The salary due over the notice period is an estate claim. Payment of salary during the notice period (a maximum of six weeks) is also guaranteed by the UWV. Holiday allowance and pension contributions that have remained unpaid are guaranteed by the UWV for a period of up to one year.

The procedure concerning termination of employment contracts is as follows.

The bankruptcy trustee has the right to terminate the employment contracts of the debtor's employees without obtaining a permit from the UWV, albeit with a notice period of a maximum of six weeks regardless of whether a longer notice period is applicable pursuant to Dutch labour law or has been agreed upon between parties. To terminate any contracts with employees, the bankruptcy trustee requires authorisation from the supervisory bankruptcy judge.

This procedure is different for collective redundancies. A bankrupt trustee who intends to terminate the employment contract of 20 or more of the employees within one UWV district within a period of three months has to inform the labour unions and if requested the UWV. In addition, the bankruptcy trustee must consult the works council. The same procedure is applicable when the bankruptcy trustee intends to transfer the ownership of the business.

During the suspension of payment, the regular dismissal rules will apply, requiring the trustee to obtain a permit from the UWV or court involvement to effect unilateral dismissals. This in practice makes the suspension of payment procedure a less efficient restructuring tool if a large number of employees are involved.

### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

A distinction should be made between the employer's and employee's part of the pension contribution and whether the premium has fallen due before or after the date of the bankruptcy.

Pension contributions falling due before the bankruptcy that have been withheld by the employer from the employee's salary, but which have not yet been paid to the pension provider, are considered to be directly based on the employment agreement and are therefore preferred claims (see question 34). The employer's part of the pension premiums will be considered an unsecured claim by the pension trustee against the employer. In practice, the UWV will be confronted with this difference in treatment of the two parts of the pension contribution as pension premiums (both the employer's and the employee's part of the pension contribution) are covered by the wage guarantee for a period of one year.

Post-bankruptcy pension-related claims, such as unpaid pension contributions that have fallen due after the bankruptcy order, are estate debts based on article 40(2) of the Dutch Bankruptcy Act.

Back-service obligations will be considered estate debts if they became payable as a result of an act by the bankruptcy trustee (in practice, as a result of a termination of the employment agreement after the date of the bankruptcy order) and an unsecured debt in all other cases.

### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

In principle, liability for environmental damage rests on the person who has caused that damage. Under Dutch law, however, remedial obligations for environmental pollution may also arise for a landowner, a land lessee, or the holder of a permit as well as the entity that caused the contamination. Generally, liability for (soil) pollution or remedial obligations, or both, may arise out of:

- contracts with the landowner regarding the use of its premises, including land lease contracts;
- conditions attached to a permit; and

- administrative remedial action, soil investigation and orders under the Soil Protection Act.

Dutch case law in respect of remedial costs for a lessor to remove contaminated goods from a property at the moment a Dutch bankruptcy trustee terminates the lease agreement (after bankruptcy of the lessee) has shown that such costs used to be classified as estate claims. On the basis of recent case law it is probable that claims are no longer to be classified as estate claim which has priority ranking but instead as an unsecured claim.

There are fines for corporations that are not in the possession of the right permits (for example, under the Soil Protection Act) or which breach environmental laws. Liabilities in relation to pollution and administrative clean-up costs depend on the severity of the pollution and the remedial costs.

Case law has shown that, in certain circumstances, other entities within the group could also be held liable for remedial costs.

The EU Directive on Environmental Liability (2004/35/EC) contains an option for national governments to implement measures on the obligation to provide financial security to cover liability risk for environmental damages. No such general measures have been implemented in the Netherlands. However, some specific legislation does include the obligation to provide financial security under certain circumstances, examples (among others) can be found in the Soil Protection Act (in the event of remedial actions at the moment of transfer of land or lease or on the basis of a remedial action plan, however, this then needs to be further specified in a general measure), the Activity Decree Environment Management (underground tank storage) and the Nuclear Energy Act (when dismantling a facility).

#### Liabilities that survive insolvency proceedings

##### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

A distinction should be made between bankruptcy and a suspension of payment.

##### 'Suspension of payments'

If a suspension of payment is successfully terminated, this means that a reorganisation plan has become binding upon the creditors bound by the plan - in broad terms, the unsecured creditors. Pursuant to the plan, the creditors may receive payment in respect of (part of) their claim. To the extent that the creditors only receive partial payment of their original claim under the plan, the remainder of their claim, as a result of the plan becoming binding, cannot be enforced against the debtor. However, the remaining part of the unpaid claim will continue to exist as an unenforceable claim.

#### Bankruptcy

In bankruptcy, three different scenarios are possible:

- The termination of the bankruptcy following acceptance of a reorganisation plan between the creditors and approval of the plan by the court: in that event, the creditors will be entitled to receive payment under and in accordance with the plan and the remainder of their claim will continue to exist as an unenforceable claim.
- Termination of the bankruptcy following a meeting of creditors and the creditors' list becoming binding: in this scenario, the assets of the debtor will have been liquidated and distributed to the creditors and the bankruptcy will have terminated. However, the records of the creditors' meeting and the final distribution list as approved by the court form an enforceable title for creditors recognised at the occasion of the meeting of creditors, which can be enforced by each of such creditors against the debtor for the remainder of their claim following receipt of their distribution pursuant to the distribution list if ever any new assets of the debtor were to surface. In addition, any party of interest may petition the court to order the former bankruptcy trustee to distribute such new, previously unknown, assets in accordance with the original distribution list or to again apply for bankruptcy of the creditor; however, in that event, new creditors of the debtor will compete for the assets.
- Termination of the bankruptcy in the absence of assets without a final distribution list having been established: in this scenario, each creditor may again individually seek recourse against any assets

that it is able to trace. Also, new applications for bankruptcy may be filed, but if a new application is filed within the three years following termination of the original case, the applicant must provide evidence that there are sufficient assets available to pay for the costs of the bankruptcy. Following termination of the bankruptcy of a legal entity for lack of assets, the legal entity will cease to exist. Alternatively to reapplying for bankruptcy, a creditor may also seek the liquidation of the company if a new asset has surfaced. If dissolution is sought by a creditor, the liquidator will be appointed by the court (see question 9).

#### Distributions

##### 38 How and when are distributions made to creditors in liquidations and reorganisations?

The bankruptcy trustee is in principle authorised to make payments to estate creditors, the tax authorities and the social security board and certain other preferential creditors or force-creditors. Force-creditors are creditors which have a strong position because of the dependency of the debtor on their services (for example, a supplier whose products are essential to the business). Unsecured creditors can only be paid after the supervisory judge has ordered interim distributions. The bankruptcy trustee will prepare a plan for distributions, which needs to be approved by the supervisory judge.

A 'suspension of payments' does not affect the rights of secured or preferential creditors. Payments to unsecured creditors can be made at any time, provided those payments are made pro rata.

#### Transactions that may be annulled

##### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

##### Outside insolvency

Outside bankruptcy, creditors can take action against voluntary legal acts performed by the debtor if both the debtor and the counterparty knew or ought to have known that the creditors of the debtor would be disadvantaged as a result of such an act. A creditor - secured or unsecured - that is prejudiced in its recourse against the debtor can void such legal act which it can do by sending a simple letter, while if the challenge is disputed, litigation will follow where the creditor has to prove that the requirements for the challenge have been met. The creditor can only do so for its own benefit and only to the extent necessary to ensure that it is no longer prejudiced.

##### 'Suspension of payments'

In a 'suspension of payments' the administrator does not have a specific statutory right under the Bankruptcy Act to void transactions.

#### Bankruptcy

In bankruptcy, the bankruptcy trustee has the right to challenge certain legal acts.

The bankruptcy trustee has the right to challenge voluntary legal acts (ie, acts where there was no prior legal obligation to perform them) for consideration, and legal acts without consideration that were performed by the debtor. In order to successfully invoke the challenge, the following requirements must be satisfied:

- the legal act of the debtor adversely affected the possible of recourse of one or more of its creditors (such disadvantage must be apparent at the time the challenge is invoked or contested in court);
- the debtor knew or ought to have known the legal act would adversely affect the possible recourse of one or more of the creditors (generally believed to be the case when the insolvency of the debtor was probable at the time of the legal act); and
- if the legal act was for consideration, it is also required that the counterparty to the transaction knew, or ought to have known, that legal act would prejudice the interests of one or more of the creditors.

The bankruptcy trustee can void such legal acts, with the effect that the act is deemed never to have occurred. The counterparty will be liable for any damage to the estate if the act cannot (wholly or partially) be unwound. For the applicable suspect periods please see question 40.

The bankruptcy trustee must prove that the requirements mentioned in the previous paragraph are satisfied in order to annul voluntary legal acts for consideration and legal acts not for consideration. Under certain circumstances, however, there is a shift in the burden of proof to the advantage of the bankruptcy trustee. This results in the presumption that both parties to the transaction knew or ought to have known that prejudice to creditors would be the result of this legal act, thereby satisfying the second and third requirements above. This presumption is rebuttable. First, specific circumstances need to be satisfied in order for the presumption to be triggered. Among these are when legal acts are performed in relation to insiders such as group companies and legal acts that result in a transaction in which the consideration because of bankrupt's counterparty substantially outweighs the consideration for the transaction received by bankrupt. Second, the following circumstances need to be satisfied:

- the legal act that adversely affected one or more creditors was performed in the year prior to the invocation of the annulment; and
- in the case when the legal act was for a consideration, the debtor must not have committed itself to that legal act before the beginning of such period (ie, the act was voluntary).

In addition, the bankruptcy trustee is able to void legal acts that were performed on the basis of a prior legal obligation, if the bankruptcy trustee can show evidence that:

- the other party knew that a petition for bankruptcy was already filed at the time that the act was performed, and the debtor was subsequently declared bankrupt; or
- the performance of the act was a result of consultations between the debtor and the other party with the aim of preferring the counterparty over the other creditors.

Note that the FSA specifically provides that it is not possible to set aside or annul the transfer of assets, rights or liabilities that has taken place between a failed entity (a bank or investment firm) and a third party, if this transfer is a result of the application of a resolution measure under the new (EU) legislative framework regarding the recovery and resolution of credit institutions and investment firms. This restriction on the *pauliana* action applies to the possibility to challenge transactions in both a pre-bankruptcy situation and the bankruptcy situation.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The ability to set aside transactions in bankruptcy is set out in question 39. There is a type of suspect period: if certain voluntary actions were performed in the year preceding the bankruptcy, two rebuttable statutory presumptions apply that relieve the burden of proof on the bankruptcy trustee. The presumptions provide that, for actions performed during that one-year period, it is deemed that such actions are prejudicial to the creditors of the debtor, and that both the debtor and the counterparty were aware of this. These actions include transactions where the value of the obligation of the debtor considerably exceeds the value of the obligation of the counterparty, or where the debtor and the counterparty are connected.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

As a general rule, managing directors of Dutch companies (the directors) are not liable for the obligations of the company. There are, however, certain exceptions to this rule. Directors of a company (and certain other legal entities) can be held personally liable for (certain) debts of the company. This would include the following situations:

- Personal liability can result because the directors have neglected to properly discharge their fiduciary duties as regards the company. This action can only be initiated by or on behalf of the company

(and in the case of bankruptcy, by the bankruptcy trustee on behalf of the company).

- Upon bankruptcy (but not in the case of a suspension of payments), the bankruptcy trustee can hold all directors of a company personally liable on a joint and several basis for the entire deficit of the bankruptcy (ie, for all costs of the bankruptcy and the amount of debt that remains unpaid after liquidation of the assets) if the board of directors has manifestly improperly performed its duties during a period of three years preceding the bankruptcy, and if it is plausible that such improper performance is an important cause of the bankruptcy of the company. If the board of directors has failed to comply with its obligation to conduct a proper administration or to publish the annual accounts in accordance with statutory requirements, the directors are deemed to have performed their duties improperly and it is presumed that the improper performance of duties constitutes an important cause of the bankruptcy. This ground for personal liability applies not only to managing directors but also to non-executive directors (supervisory board directors; if, for example, they have failed to properly supervise the managing directors in relation to their obligations to maintain a proper administration and file annual accounts in a timely manner).
- Directors can be held personally liable for unpaid taxes and social security contributions. In particular, directors of a company in financial distress must notify the tax authorities and the social security board in writing if the company is no longer able to pay certain taxes, including VAT, wage withholding tax and social security contributions that are due. This notification should be made within two weeks of the date that the taxes and social security contributions should have been paid, and a failure to do so may result in the directors being held jointly and severally liable if the taxes and social security contributions remain unpaid. If a valid notice has been given, directors will only be liable if they have manifestly performed their duties improperly during a period of three years preceding the bankruptcy and if it is plausible that such improper performance is an important cause of the bankruptcy of the company.
- Directors (and even shareholders) may, in certain circumstances, be liable to creditors of the company or other parties on the basis of tort, for example, if the directors created a false representation of creditworthiness of the company or knowingly entered into transactions when they knew or ought to have known that the company was not going to be able to perform its obligations.
- Criminal liability may apply, for instance, in situations where managing directors fraudulently withheld assets of the company from the bankruptcy trustee or manipulated the accounts of the company to deceive investors or creditors.

Because of recent legal developments in the Netherlands, the bankruptcy of a company can – under certain circumstances – have severe legal consequences for its directors if directors' duties have not been properly observed.

Following the entry into force of the Director Disqualification Act on 1 July 2016, the Bankruptcy Act now grants the bankruptcy trustee or the Public Prosecution Service the authority to request the court to disqualify a director of a bankrupt company for a maximum duration of five years, if certain acts have been perpetrated by the director. A director who is disqualified following such a request, is prohibited to act as a director of a legal entity for the duration set out in the court order.

In addition, the Penalisation of Bankruptcy Fraud Amendment Act entered into effect on 1 July 2016. This Act extended the scope of the criminal liability of (supervisory) directors, for instance to situations where:

- a director fails to keep a proper administration of the company or, in the event of bankruptcy, intentionally does not provide the bankruptcy trustee with such administration; and
- a director excessively uses, withholds, disposes of the company's assets and resources or has granted a creditor an undue preference, which prejudices one or more creditors of the company.

See 'Update and trends' for more information about the Director Disqualification Act and the Penalisation of Bankruptcy Fraud Amendment Act.

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**Groups of companies**
**42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

The basic premise is that shareholders are not liable for debts of group companies or subsidiaries. Shareholders can, however, be held liable in connection with the debts of subsidiaries or group companies when the shareholder has committed a tort with regard to the creditors by infringing on a duty of care. The following circumstances are prerequisites to a duty of care being established:

- the shareholder must have control over the subsidiary. Factors that can indicate control over the subsidiary include:
  - a majority shareholding;
  - the articles of association of the subsidiary;
  - the existence of personnel unions; and
  - the employment contract of the director of the subsidiary, which may for instance include a power of the parent company to instruct the director of the subsidiary;
- the shareholder is involved in the business of the subsidiary, for instance through the presence of a cash management system; and
- the controlling shareholder has insight into the lack of recourse available to the subsidiary for the satisfaction of the creditors of the subsidiary, but nonetheless permits the subsidiary to continue to trade.

Whether a shareholder has a duty of care to the creditors of a subsidiary or group company depends on the circumstances of the individual case. If there is central cash management through the controlling parent, the parent will generally have a sufficient level of knowledge as to the financial position of the subsidiary for liability to arise.

On the basis of case law, the supervisory judge in insolvency proceedings is able to allow consolidated liquidation for two or more entities that are declared bankrupt. This type of liquidation entails that the various bankruptcies are treated as one insolvency procedure. This will only happen in extraordinary cases.

When there is a matter of group liability, for example, when more than one company has taken an action which caused damage and it is not traceable which action specifically caused the damage, this liability may be joint and several. This means the creditor of such damage can recover its damage as a whole from any entity that is part of the group.

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**Insider claims**
**43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

Insiders should abstain from setting off claims where the insolvency of an affiliated company is expected. Claims or debts following the transfer of these claims or debts prior to the declaration of bankruptcy or suspension of payment may under certain circumstances not be set off against the estate. A person who has assumed a debt towards the bankrupt or acquired a claim against the bankrupt from a third party is not allowed to set off such debt or claim if, at that time, he or she knew that, in view of the financial situation of the insolvent entity, the bankruptcy or 'suspension of payments' of the entity was to be expected (see question 17).

In addition, the Dutch Bankruptcy Act limits the possibility of setting off claims that are acquired before the date of bankruptcy, but where the acquirer was not acting in good faith, which is the case if the acquirer knew that the financial position of the insolvent entity was such that bankruptcy or a suspension of payment was to be expected.

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**Creditors' enforcement**
**44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

A mortgagee and a pledgee or a security holder under a financial collateral arrangement can foreclose on the secured assets if there is a default in the performance of the secured obligations. For more detail, see questions 6 and 7. Unsecured creditors can levy an attachment (see question 8).

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**Corporate procedures**
**45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

Yes. Under corporate law a company can be dissolved. In most cases, the company is dissolved pursuant to a shareholders' resolution. The shareholders will appoint a liquidator, who will liquidate (all assets of) the company. However, if it becomes apparent that the liabilities of the company will exceed the assets of the company, the liquidator is obliged to file for the bankruptcy of the company, unless all known creditors agree with the continuation of the corporate liquidation proceedings.

An important difference to bankruptcy is that the corporate liquidation proceedings are, in principle, not court-supervised.

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**Conclusion of case**
**46 How are liquidation and reorganisation cases formally concluded?**

Voluntary liquidation (see question 45) terminates as a result of:

- a declaration of bankruptcy being made pursuant to an application for bankruptcy by the liquidator; or
- payment of the final distribution to creditors and shareholders of the company being made.

Suspension of payments terminates as a result of:

- revocation of the 'suspension of payments' and conversion into bankruptcy (this can happen in a number of situations, including when the debtor acts in bad faith when administering the estate, if the debtor tries to bind the estate without the approval of the administrator, or when it becomes clear that the 'suspension of payments' will not result in the repayment of debts or a reorganisation plan with the creditors);
- lapse of time;
- refusal of creditors to grant a definitive suspension of payments;
- approval by the court of a reorganisation plan, the approval of which has become conclusive; or
- payment of all debts.

Bankruptcy terminates as a result of:

- a successful appeal against the verdict declaring the company bankrupt;
- a court decision terminating the bankruptcy as a result of insufficient funds to pay unsecured creditors;
- approval by the court of a reorganisation plan, the approval of which has become definitive;
- payment of all debts; or
- a final distribution to creditors being made if the list concerning the distribution to creditors has become definitive, regardless of whether all creditors have been paid.

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**International cases**
**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

As a result of the EU Insolvency Regulation, the opening of insolvency proceedings in one of the EU member states (except for Denmark) and the effects thereof are also directly recognised in the Netherlands, unless secondary or territorial insolvency proceedings are opened in the Netherlands. See the chapter on the European Union.

The effects of the opening of insolvency proceedings in other non-EU jurisdictions (including Denmark, which has opted out of the EU Insolvency Regulation) are only to a certain limited extent recognised in the Netherlands. This recognition may be challenged if the principles of due process and fair trial have not been observed in the foreign procedure. In the absence of a treaty and where the EU Insolvency Regulation does not apply, the Dutch Supreme Court has consistently

## Update and trends

### The Director Disqualification Act

The Director Disqualification Act entered into force on 1 July 2016. The bankruptcy trustee of a bankrupt company or the Public Prosecution Service can request a court to disqualify a director of a company, for a maximum period of five years.

At the request of the bankruptcy trustee or the Public Prosecution Service, a court can disqualify a director of a company if in the period of three years prior to the company's bankruptcy:

- pursuant to a final and conclusive court order, the director is held liable for the bankruptcy of a company because of mismanagement and that the mismanagement was an important cause of the company's bankruptcy;
- the director knowingly performed or permitted legal acts on behalf of the company that prejudiced creditors of the company, and the acts were subsequently nullified by a court in accordance with the Bankruptcy Act;
- the director has severely failed in complying with his or her statutory cooperation and information duties (under the Bankruptcy Act) vis-à-vis the bankruptcy trustee;
- the director has been involved in a bankruptcy at least twice, and serious blame can be attributed to the director with respect to these prior bankruptcies; or
- pursuant to a final and conclusive ruling the company or its director have been fined for certain violations under Dutch tax law.

The director can be disqualified for a maximum period of five years. During this period he or she cannot act as a director or supervisory board director of any legal entity (unless the court order states otherwise). Upon a final and conclusive decision on the matter (by either the court in first instance or higher courts in the event of an appeal), the disqualification of the director will be registered in the trade register of the Dutch Chamber of Commerce until the end of the term of the disqualification. Civil law notaries and the Dutch Chamber of Commerce are prohibited from cooperating with the incorporation of a legal entity if one of the intended directors is registered as a disqualified director. Any appointment as a director or supervisory board director who was disqualified following a final and conclusive court order will be void by operation of law. In the event the disqualification of its director/supervisory board director would cause a company to be left without a director or supervisory board director, then the court can decide to appoint a temporary director or supervisory board director.

The scope of the Director Disqualification Act extends to (former) directors of legal entities (such as private or public limited liability companies, foundations, a cooperation) that are incorporated under the laws of the Netherlands (including *societas Europae* (European companies)) and that have their registered office in the Netherlands as well as to natural persons that are conducting (or have conducted) a profession or business. Under Dutch law a director of a company also entails a de facto director, who is not officially appointed as a director pursuant to the articles of association of a company. A disqualification under the Director Disqualification Act can only be imposed:

- in relation to a bankruptcy declaration after 1 July 2016; and
- with regard to facts and circumstances that came into existence after 1 July 2016.

### The Penalisation of Bankruptcy Fraud Amendment Act

This Act entered into force on 1 July 2016 and aims to combat, among other things, bankruptcy fraud. The Act also penalises wilful non-compliance with the duty to keep proper records or to provide information to the bankruptcy trustee.

A director (including the de facto directors) or supervisory board directors (hereafter 'director') can be held punishable under the Penal Code, resulting in prison sentences of up to six years or fines of up to €82,000. In addition to existing criminal liability for directors under the Penal Code, the following scenarios are now punishable following the entry into force of the Penalisation of Bankruptcy Fraud Amendment Act:

- if the company's financial soundness was endangered by a director's excessive use or disposal of the company's resources (including permitting or cooperating with such acts);
- if prior to the company's bankruptcy, prejudice to the recourse options of one or more creditors of the company is caused by:
  - the director's excessive use or disposal of the company's resources (including permitting or cooperating with such acts);
  - the director fraudulently withdrawing any asset from the company's estate; or

- the director granting one creditor of the company an undue preferential treatment;
- if during or prior to the company's bankruptcy:
  - a breach of the duty to keep a proper administration is caused intentionally by the director, or attributable to his or her actionable negligence; and
  - if during the bankruptcy of the company, the director intentionally breaches his or her statutory duty to cooperate or provide information;
- provides incorrect or incomplete information; or
- breaches his or her duty to immediately provide the bankruptcy trustee with the company's administration.

### The Pre-pack legislative proposal

The pre-pack procedure, which was developed/applied in the legal practice but lacked a statutory foundation, has now been codified in a legislative proposal: the Continuity of Companies Act I. The proposal was accepted by the House of Representatives on 21 June 2016 and is currently being reviewed by the Senate. Assuming that the current proposal is accepted by the Senate, the new legislation will introduce a system in which debtors in financial distress (not being banks, insurers or natural persons who are not carrying out a business) are able to prepare and attempt a silent reorganisation/restructuring of the debtor's business through a pre-pack procedure. The pre-pack phase allows the debtor, together with the court-appointed bankruptcy trustee designate and the most important (secured) creditors, to explore and prepare, for example, an asset sale or other restructuring measures, which can subsequently be implemented immediately upon the commencement of the formal insolvency procedure. During the pre-pack phase, the debtor remains authorised to manage and dispose of its assets.

The pre-pack procedure may only be requested by the debtor, who must be represented by a lawyer. The court will allow the debtor to enter the silent preparation phase only if the debtor proves the added value of the pre-pack procedure to the specific situation at hand. If the debtor's request is granted, then the court appoints one or more bankruptcy trustee designates and one or more intended supervisory judges. The bankruptcy trustee designate must act in the interest of the debtor's creditors, but he or she does not need to follow instructions from these creditors or from the debtor himself or herself. He or she is supervised by the intended supervisory judge.

If the debtor has a (statutorily required) works council or employee representative body, then the debtor must involve that representative body in the pre-pack procedure (unless this is against the interest of the debtor's company; note that any works council member or employee representative that is involved is bound by a duty of confidentiality). Further, the court may, at its own discretion, stipulate that the pre-pack phase is subject to certain conditions if the court deems such conditions necessary to achieve the statutory aim of the pre-pack procedure, enhance the position of the bankruptcy trustee designate or protect the interests of the debtor's employees.

The pre-pack commences as soon as the court has appointed the bankruptcy trustee designate. In principle, the bankruptcy trustee designate is appointed for a term of two weeks. At the debtor's request, this period can be extended. After having heard the intended supervisory judge and bankruptcy trustee designate, the court decides whether or not to grant the debtor's extension request, and if so, the term of the extension. The court's decision on the debtor's pre-pack request or an extension request cannot be appealed.

By operation of law the pre-pack ends when the appointment term of the bankruptcy trustee designate expires, or when the debtor is declared insolvent (ie, bankruptcy or suspension of payment). The court can also decide to end the pre-pack phase or attach certain conditions to the pre-pack phase, at the request of the bankruptcy trustee designate, the intended supervisory judge or a creditor. The court decides upon such request, after having heard the debtor, one or more creditors, the bankruptcy trustee designate and the intended supervisory judge.

The legislative proposal for the pre-pack procedure is currently awaiting approval by the Senate. It is expected to enter into effect in 2017. Currently, there are ongoing proceedings regarding the pre-packaged sale of a large provider of childcare facilities. In these proceedings the Dutch court referred preliminary prejudicial questions to the European Court of Justice in February 2016. In essence, the questions come down to whether or not Directive 2001/23/EC (for further detail see the chapter on the European Union) safeguarding employees' rights in the event of transfers of undertakings, businesses or parts of undertakings or businesses applies to the pre-pack procedure or not.

decided that, foreign insolvency proceedings only have a ‘territorial effect’, meaning that they do not affect the debtor’s assets located in the Netherlands and the legal consequences attributed to the bankruptcy pursuant to the bankruptcy law of such foreign country cannot be invoked in the Netherlands to the extent that it would result in any unpaid creditors no longer being able to take recourse on the assets of the debtor located in the Netherlands (either during or after the relevant foreign insolvency proceedings). This does, however, not imply that the powers of a foreign bankruptcy trustee are not being recognised in the Netherlands. In Dutch case-law it is determined that a foreign insolvency office holder is allowed to invoke its rights as available pursuant to the foreign domestic insolvency law, including over assets that are located in the Netherlands. The office holder is also allowed to sell these assets and consider the proceeds part of the assets of the foreign bankruptcy estate. Notwithstanding that the foreign insolvency procedure’s seizure is regarded as having only territorial effects of the foreign insolvency, the effects are de facto recognised in the Netherlands, because the foreign insolvency office holder is able to exercise its power under the *lex concursus*.

Creditors are allowed to individually take recourse against the debtor’s assets situated in the Netherlands, notwithstanding the opening of insolvency proceedings against the debtor abroad. Foreign creditors are, in general, not treated differently from creditors that are incorporated or residing in the Netherlands.

The Netherlands has not adopted the UNCITRAL Model Law on Cross-Border Insolvency and this is not currently under consideration.

## COMI

### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

The definition of COMI derives from European Union law. There is a general presumption that a debtor’s COMI is in the place of its registered office. This is slightly modified in the Regulation Recast which states that it is not possible to rely on the rebuttable presumption where a debtor has moved its COMI in the three months prior to insolvency proceedings. See further the chapter on the European Union.

In practice the Dutch courts have, among others, considered the following factors:

- the fact that the business activities of a Dutch general partnership had transferred to a foreign company which had been set up by the (general) partners did not result in the COMI of the Dutch general partnership no longer being located in the Netherlands;
- in respect of a company that for a considerable time no longer engaged in economic activities in the Netherlands, there was no longer any actual functioning COMI in the sense of the EU Insolvency Regulation and therefore only the statutory seat of the company was relevant in determining the COMI; the fact that liquidation activities were taking place in another EU member state was

in this case not relevant as these were no (economic) activities of the company;

- the fact that the company’s largest creditors were located in the Netherlands; that it was part of a Dutch fiscal unity; the court did not find relevant that the company had plans to move its statutory seat to another EU member state for tax reasons, as the test date is the date of the request for the opening of the insolvency proceedings;
- the fact that a company is also registered in another EU member state did not mean that the registration and statutory seat in the Netherlands had ended (and that therefore the COMI was no longer in the Netherlands);
- the fact that the most important activity of a company was the holding of shares in another company (in another EU member state), which was conducted from the Netherlands (the company paid tax in the Netherlands, with returns administered by a Dutch trust company and Dutch accountant, accounts were drawn up and deposited in the Netherlands and general shareholder meetings were held in the Netherlands on the basis of the articles of association);
- the fact that the tax returns were addressed by the Dutch tax authorities to an address in another EU member state and that the accounts were (also) prepared by an administration office in another EU member state did not result in COMI in another EU member state; and
- the fact that the company did not have a visiting address in the Netherlands and that monies were lent through the company (using foreign bank accounts) to avoid lending in another EU member state also did not lead to the COMI no longer being in the Netherlands.

In accordance with European Union law, Dutch courts determine the COMI for each individual company within a group of companies. This is apparent, for example, in a judgment in which the Dutch court decided that the COMI of three subsidiaries of a Dutch company in another EU member state was not relevant, as it looked at the debtor (the Dutch company) for the determination of a the COMI as a separate legal entity – even if the debtor has an interest in these activities of its subsidiaries. However, in Dutch practice, occasionally one bankruptcy trustee may be appointed for various subsidiaries within a group that all have its COMI in the Netherlands to facilitate the group being restructured as a single unit.

## Cross-border cooperation

### 49 Does your country’s system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

In respect of the recognition of foreign insolvency proceedings, see question 45.



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The EU Insolvency Regulation provides an obligation for cooperation and information exchange between insolvency office holders. See further the chapter on the European Union.

Cooperation between domestic and foreign courts or domestic and foreign insolvency administrators is not explicitly dealt with in the Dutch Bankruptcy Act. The Act does not prohibit and can provide a basis for coordination between procedures. Also in practice coordination or cooperation does occur and cross-border insolvency agreements (protocols) have been used.

An example of cooperation between different countries (including the Netherlands) in a cross-border insolvency is the insolvency of the Lehman Group. A cross-border insolvency protocol was agreed with the aim of cooperation between the trustees and liquidators of the different entities of the Lehman Group, in view of the common interest of the creditors. Furthermore, the aim of the protocol was to reduce the costs of settlement to a minimum and to share information. The bankruptcy trustee for Lehman Brothers Treasury Co BV signed up to the protocol as he considered this to be in the best interest of the Dutch entity's creditors (no court consent was required).

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**Cross-border insolvency protocols and joint court hearings**

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- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

Dutch trustees in bankruptcy do enter into cross-border insolvency protocols. However, to date, there have been no cross-border insolvency protocols entered into between Dutch courts and foreign courts. Also, no joint hearings have been held to date, although the Dutch (lower) courts have recognised the voting outcome of Chapter 11 hearings in the United States for the purposes of voting on a reorganisation plan in a Dutch suspension of payment.

# Nigeria

Emmanuel Ekpenyong and Cinderella Agunanna

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

Insolvencies and reorganisations of companies are generally governed by the Companies and Allied Matters Act (CAMA) Cap, C 20, Laws of the Federation of Nigeria, 2004 and the Companies Winding-up Rules.

The Investment and Securities Act 2007 and Securities and Exchange Commission Rules 2013 regulate mergers, takeover and acquisitions of shares in publicly quoted companies in Nigeria.

The Banks and other Financial Institutions Act (the BOFIA), Cap B3, Laws of the Federation of Nigeria, 2004 regulates restructuring, reorganisation, mergers and disposal of banks.

The Nigeria Deposit Insurance Corporation Act, Cap N 102, Laws of the Federation of Nigeria, 2004 regulates insurance of deposit liabilities of licensed banks and other financial institutions to protect interest of depositors in the event of imminent or actual financial difficulties of banks.

The Assets Management Corporation of Nigeria Act, 2010, which was amended by the Assets Management Corporation of Nigeria (Amendment) Act, 2015, established the Assets Management Corporation of Nigeria (the Corporation) for the purpose of efficiently resolving non-performing loan assets of banks.

The Bankruptcy & Insolvency (Repeal and Re-enactment) Act 2016 (the Bankruptcy Act) and Bankruptcy Rules regulate bankruptcy proceedings in Nigeria.

Section 408(d) provides that a company is insolvent if it is indebted to its creditors;

- in a sum exceeding 2,000 naira and is unable to pay same upon service of three weeks' statutory notice on it;
- upon execution of judgment against and it is returned unsatisfied in whole or in part; or
- where the court considers the liability of the company and is satisfied that it is unable to pay its debts.

Nevertheless, under section 411(2) of the CAMA, the court may refuse to grant a winding-up order against a company on the ground of insolvency if it is not reasonable to do so, or the petitioners have an alternative remedy, or if it is not just and equitable to do so.

Section 4 of the Bankruptcy Act provides that a person commits acts of bankruptcy if he or she, either in Nigeria or abroad, makes an assignment to a trustee for the benefit of creditors, makes fraudulent gift or transfer of property, transfers property that is interpreted to be a fraudulent preference under the Act, leaves Nigeria and remains abroad with intent to defraud his or her creditors, fails to redeem his or her property after 21 days of seizure pursuant to an execution, discloses to his or her creditors statements that he or she is insolvent and gives notice that he or she is about to suspend payment of debts to his creditors.

Section 5 of the Bankruptcy Act states that a creditor may file a bankruptcy petition if the debtor owes him or her a sum of up to 1 million naira or commits an act of bankruptcy within six months before presenting the petition.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Section 7 of the Federal High Court Act, Cap F12, Laws of the Federation of Nigeria, 2004 and section 251(1)(e) of the Constitution of the Federal Republic of Nigeria, 1999 (as amended) confers jurisdiction to hear insolvency proceedings to the Federal High Court, with judicial divisions in each state of the federation.

The company's creditors and contributories may institute legal proceedings to recover claims against the company before or during winding up of a company at the state High Court with jurisdiction to hear the claims.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The provisions of the CAMA are applicable to the winding up of an insurance company subject to the provisions of the Insurance Act 2003. Section 32(1) of the Insurance Act provides for the winding up of an insurance company upon the petition of either 50 policyholders who have held a policy for not less than three years or the National Insurance Commission.

Section 31(4) of the Insurance Act provides that the priority of settling debts owed by an insurance company at winding up is:

- liquidation fees;
- secured creditors;
- policy holders;
- other creditors;
- staff; and
- shareholders and directors.

Section 33 of the Insurance Act prohibits the voluntary winding up of a life insurance business except for the purpose of effecting an amalgamation, transfer or acquisition.

Section 7 of the Banks and Other Financial Institutions Act prohibits the restructure, reorganisation, merger and disposal of interest in banks without the prior consent of the Governor of the Central Bank of Nigeria. It is an offence to contravene this provision.

Under the Bankruptcy Act, the debtor's assignment of his or her existing and future wages, commission or professional fees before bankruptcy does not affect his or her wages, commission and professional fees after bankruptcy. Upon the filing of the debtor's proposal, the creditors do not have a remedy against the debtor or his or her property or right of action for the recovery of claims provable in bankruptcy until the trustee is discharged or the debtor becomes bankrupt. Upon the bankruptcy of the debtor, no creditor has any remedy against the debtor or his or her property or shall commence an action for claims provable in bankruptcy until the trustee is discharged.

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**Public enterprises**


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**4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?**

Where there is a need to make a government enterprise more productive or where it is poorly managed, or to raise capital in a period of economic recession, public enterprises may be liquidated by privatising them under the Public Enterprise (Privatisation and Commercialisation) Act, Cap P38, Laws of the Federation of Nigeria, 2004. This is achieved by offering the shares of the public enterprise by public issue at the capital market or share private placement as provided for in section 2 of the Public Enterprise (Privatisation and Commercialisation) Act. The National Council of Privatisation may approve that the shares be offered for sale to a willing buyer or the shares may be disposed to interested investors through a local or international capital market.

Section 4 of the Public Enterprise (Privatisation and Commercialisation) Act provides that a privatised enterprise that requires participation by strategic investors may be managed by the strategic investors as from the date of the privatisation on terms that will be agreed upon.

Public enterprises are usually wholly owned by the government or its agencies but in the event that there are pending claims of creditors, it will be settled before the effective date of the privatisation. The creditors reserve the right to seek a restraining order against the parties to the privatisation until their claims are settled.

Under section 8, commercialised enterprises shall operate as a pure commercial enterprise and, subject to the general regulatory power of the federal government, fix the rates for goods and services, capitalise its assets, borrow money and issue debenture stocks and sue and be sued in its corporate name.

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**Protection for large financial institutions**


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**5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?**

The commercial banks are huge investments that are considered 'too big to fail'. Section 2 of Asset Management Corporation of Nigeria Act 2010 provides the Corporation with an authorised share capital of 10 billion naira wholly subscribed by the federal government and held in trust by the Central Bank of Nigeria and the Ministry of Finance for the purpose of managing and realising the takeover of bad loans of banks in Nigeria in order to keep the banks afloat and instil confidence in the Nigerian banking sector.

The Corporation has the power to dispose eligible bank assets, including the collection of interest, principal and capital due and the taking over of collateral securing such assets.

The Act also empowers the Corporation to apply to court for forfeiture of the debtor's property upon its inability to liquidate its debts.

Also to prevent commercial banks from failing, the share capital of commercial banks was increased from 2 billion naira (about US\$ 6.5 million) to 25 billion naira (about US\$81.9 million). The restructuring, reorganisation, merger and disposal of banks are effected under the supervision of the Central Bank of Nigeria and consent of its governor. Under section 31 of the BOFIA, the governor of the Central Bank of Nigeria shall appoint a director of bank supervision to carry out supervisory duties in respect of banks, other financial institutions and specialised banks.

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**Secured lending and credit (immovables)**


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**6 What principal types of security are taken on immovable (real) property?**

Security on immovable real property is a legal mortgage, charged by way of debenture or a charge on the property in urban areas. Legal mortgage is a security document that protects a lender's rights under a loan. A legal mortgage transfers the title in the property to the lender who may exercise the right of foreclosure and sale without commencing legal proceedings where the borrower is in default of payment.

A charge is a medium of securing debt. It does not transfer the title to the property to the lender. Nevertheless, the lender may enforce the agreement with the borrower by legal proceedings.

Legal mortgage and charge are registrable instruments in most jurisdictions in Nigeria. Where the borrower is a company, the legal

mortgage or charge is filed at the Corporate Affairs Commission (the Company Registry) by filing Form 8 (Particulars of Mortgage or Charge) to notify investors of a charge against the company's assets.

Security on immovable (real) property in rural areas is mostly pledges and equitable mortgage. A pledge is a possessory right in which a borrower grants a lender over the property as security for a loan. In equitable mortgage, the borrower deposits the title documents with the lender to secure the loan. The courts have held inchoate legal mortgage to be equitable mortgage.

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**Secured lending and credit (moveables)**


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**7 What principal types of security are taken on moveable (personal) property?**

The security on moveable personal property is charged on the property itself.

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**Unsecured credit**


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**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

An order for liquidation operates in favour of all the creditors whether secured or unsecured as if made on a joint petition. Nevertheless, secured creditors' claims take priority over unsecured creditors' claims. This is because an unsecured creditor only benefits from insolvency proceedings in the likely circumstance that there is a remainder from the sale of the company's assets after settling the claims of the secured creditors.

Nonetheless, the unsecured creditors have a right to commence an action against the liquidator or official receiver of the company and attach its property to satisfy an unsecured claim. Again, where the debt is a liquidated sum, the creditor may commence a summary judgment action to recover the sum. In this instance, the creditor may enforce the judgment against the company through writ of *fifa*, attachment of immovable property, garnishee proceedings or judgment summons in appropriate cases. The unsecured creditor may also apply to the court hearing the liquidation proceedings to adjourn the hearing of the liquidation petition.

Under the CAMA and the Bankruptcy Act, a foreign representative may maintain proceedings in Nigeria as a creditor, contributory, trustee, liquidator or receiver of the debtor. The claims will be considered by the court in order of the priority of claims. Section 238 of the Bankruptcy Act provides that where there is a bankruptcy or insolvency, reorganisation order made against a debtor in a foreign proceeding, a certified copy of the order is, in the absence of contrary evidence, proof that the debtor is insolvent and appointment of a foreign representative has been made. In such an instance, upon an application of the foreign representative, the court may limit the property in which the authority of the Nigerian trustee extends. On application by a foreign representative in a Nigerian court in respect of a foreign proceeding commenced for the purposes of effecting a composition, an extension of time or a scheme of arrangement, the court may grant a stay of proceeding against the debtor.

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**Voluntary liquidations**


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**9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?**

Under Section 457 of CAMA, voluntary liquidation is commenced when:

- the duration for the company as stated in its article expires;
- the occurrence for which the articles provide for the company to be dissolved has occurred; or
- the company in a general meeting passes a special resolution for the company to be liquidated.

Nonetheless, a creditor or contributory may apply to court to discontinue the voluntary liquidation of the company if it is against its interests.

Voluntary liquidation is an administrative process effected by:

- filing the following documents at the Company Registry;
- publication of notice of the creditors' meeting in the Gazette and two daily newspapers;

- resolution for voluntary winding up;
- appointment of a liquidator;
- publication of notice of appointment of a liquidator in the Gazette and at least two daily newspapers;
- the liquidator's notice of appointment;
- publication of a notice of final meeting in the gazette and at least two newspapers circulating in the locality of where the meeting is being held;
- return of final meeting and account of liquidation as laid before and approved by the meeting;
- original certificate of registration;
- updated annual return; and
- payment of the statutory fees.

Under section 486 of the CAMA, a creditor or contributory may petition the court after the company passes a resolution to voluntarily wind up the company, with the court supervising the winding up. Where the court grants an order for winding up of a company subject to its supervision, the court will appoint an additional liquidator who shall exercise all the powers of a liquidator without sanction or intervention of the court as if the company is wound up voluntarily. Nevertheless, in the case of creditors' winding up, the liquidator shall act with the sanction of court and committee of inspection or the creditors' meeting where there is no committee in inspection.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Under section 472, the creditors may call for a meeting to pass a resolution for voluntary winding up of the company after publishing notice of the meeting once in a gazette and two newspapers circulating where the company has its principal place of business. The directors shall upon receipt of the notice compile the statement of the company's affairs, the list of creditors and their claims before the day of the proposed meeting and appoint one of the directors to preside over the meeting. The creditors shall at the meeting appoint a liquidator who shall sell and distribute the assets of the company. The creditors will also appoint a committee of inspection who shall fix the remuneration of the liquidator. Upon appointment of the liquidator, the powers of the directors over the company shall cease. Upon winding up, the liquidator shall prepare an account showing how the winding up was effected and how the assets of the company were disposed of. The liquidator shall, in a general meeting of the company and creditors' meeting, tender the account and explain how the winding up was effected. It is an offence for the liquidator to fail to call the meetings.

The liquidators shall deliver the account and the minutes of the respective meetings to the Company Registry and same will be registered. The company shall be deemed dissolved at the expiration of three months after registration. Nevertheless, a creditor, the liquidator or a shareholder may apply to court for an order for extension of time to deem the company dissolved and deliver the order to the company registry within seven days after it was made. A person is guilty of an offence, if he or she fails to deliver the order to the company registry within seven days from the day the order was made.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Section 538 of the CAMA provides that a company may commence a formal financial reorganisation by passing a special resolution to that effect. The liquidator will be authorised to sell a part or the whole assets of the company to the transferee company in consideration or part consideration of fully paid share and distribute the sum to the shareholders in accordance with their shareholding in the company.

The consequence of a financial reorganisation will be a change in the rights or liabilities of members, debenture holders and creditors of the company or any class of them including the regulation of the company.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

There is no procedure for creditors to file for involuntary reorganisation of the company.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Where a company defaults in holding a statutory meeting; its members decrease below two or it is just and equitable to do so, the company or the Company Registry may commence mandatory liquidation proceedings against the company. Transactions by an insolvent company are invalid, and the directors engaged in such transaction would be held personally liable.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

During reorganisation, the company can carry on business through the liquidator or receiver manager. To effect the reorganisation, a company may by special resolution resolve that it be put into members' voluntary liquidation and the liquidator be authorised to sell the whole or part of its undertakings or assets to another company. The rights of the creditors of the company are not affected by the reorganisation but there is no special treatment given to creditors who supply goods or services after the filing.

The creditors or shareholders may apply to court to order a meeting of shareholders or a class of shareholders or creditors or class of creditors and the meeting would be summoned in a manner as the court may direct. If three-quarters of the shareholders or creditors present agree to any reorganisation plan by voting either in person or proxy, the plan will be referred to the Securities and Exchange Commission (SEC), which will confirm the fairness of the plan by making a written report within the time specified by the court. If the court is satisfied with the fairness of the plan, it shall sanction the same and be binding on all the shareholders and creditors.

Once a special resolution is passed and a liquidator or receiver manager appointed, the directors and officers do not have powers to bind the company.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

Once a liquidator is appointed, no action shall be commenced against the company except with the leave of court. Nevertheless, where an action is commenced after the presentation of petition, the company or creditor may apply for a stay of proceedings and the court would either stay proceedings or refer the action to the court hearing the liquidation petition.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

A company in liquidation may obtain secured or unsecured loans or credit by the liquidator or receiver manager appointed by the court, but such loan must be for the purpose of carrying on the company's

business for the period provided by the court in the liquidation order for the purpose of settling the creditors' claim.

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### Set-off and netting

- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

In the case of an unlimited company, the court may allow to a contributory by way of set-off any money due to him or her which he or she represents from the company of any independent dealing or contract with the company but not money due to him or her as a member of the company. In the case of a limited company, it is a director whose liability is unlimited who is given the same treatment as a contributory of an unlimited company.

Whether limited or unlimited when all creditors are paid in full, the money due on any account to a contributory may be allowed to him or her by way of set-off against any subsequent call.

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### Sale of assets

- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

A liquidator appointed by the court sells the company's assets 'free and clear' of claims by public auction or private contract as may be suitable in the circumstance provided that the exercise of the liquidator's power of sale is subject to the control of the court.

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### Intellectual property assets in insolvencies

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

Though the IP laws are silent on this aspect, upon commencement of a liquidation proceeding, the IP licences shall continue to be used by the company until the liquidation order is made. An IP licence is an asset of the company and may be sold alongside other company assets, in which case the new owner would continue to use the IP licence with the consent of the licensor.

A liquidator cannot terminate the company's agreement with a licensor and continue to use the IP licence for the benefit of the company in liquidation.

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### Personal data in insolvencies

- 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

There is no restriction on the use of such information in the insolvency or transfer of the company to a purchaser.

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### Rejection and disclaimer of contracts in reorganisations

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

Section 506 of the CAMA provides that if in the course of winding up of a company, the liquidator, official receiver, contributories or creditor discover that the company's officers carried out its business in a

reckless manner with intent to defraud the company, the creditors of the company or creditors of another company, the liquidator, official receiver, contributories or creditor may reject the transaction and apply to court to declare that the officers involved be personally liable without limitation to the debts or loss arising from such transaction.

The officers would be guilty of an offence and upon conviction liable to a fine and term of imprisonment of two years.

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### Arbitration processes in insolvency cases

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Insolvency matters are not subject to arbitration proceedings. This is because arbitration tribunals do not have coercive powers to make orders to bind the stakeholders of a company before and during winding-up proceedings. Moreover, it is only parties to an arbitration agreement that are subject to the jurisdiction of an arbitration tribunal. Arbitration is commonly used for resolution of commercial disputes.

However, arbitration proceedings commenced by the company against a third party or a stakeholder in the company before the commencement of liquidation proceeding will not be stayed or dismissed because proceeds from the arbitral award in favour of the company is an asset due to the company.

If the arbitral proceeding was commenced by a creditor or contributory against the company before the commencement of liquidation proceeding, he or she may file an application at the court hearing the winding-up proceeding for a stay of proceedings pending the publication of the arbitral award.

In any case, arbitrable commercial disputes that arise in an insolvency case after commencement of winding-up proceedings may be resolved by arbitration as long as there is an arbitration or submission agreement between the parties involved in the disputes.

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### Successful reorganisations

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

The reorganisation plan must be fair and equitable. See question 14.

Claims for non-debtor parties' liability may be waived except where there is fraud or wilful misconduct.

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### Expedited reorganisations

- 24 Do procedures exist for expedited reorganisations?**

No.

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### Unsuccessful reorganisations

- 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

A proposed reorganisation is defeated where:

- there is an order on the grounds of unfairly prejudicial and oppressive conduct to minority shareholders or for liquidation of the company under creditor's voluntary liquidation, the reorganisation is invalid unless sanctioned by the court;
- the creditor or any class of creditors, or members or a class of members agree on a reorganisation plan, but the SEC's written report shows that the plan is not fair or equitable; and
- where the court for whatever reason refuses to sanction the SEC's written report or the reorganisation plan.

Reorganisation upon a disapproved plan is invalid. Where the court sanctions the plan and the liquidator fails to perform the plan, a shareholder or creditor may apply to court for the plan to be performed.

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## Insolvency processes

- 26** During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

Upon service of the petition for liquidation on the company, the petitioner would seek and obtain an order of court to advertise the petition in a national daily newspaper or Official Gazette within 15 days of the hearing of the petition. The purpose of advertisement is to inform the company's creditor and persons interested in the company of the pending liquidation petition against the company.

Upon advertisement of the petition, every creditor person who intends to appear at the hearing of the petition shall file an affidavit within 15 days after the advertisement of the petition. The petitioner has five days within which to file his affidavit in response to affidavits against the petition.

In the administration and distribution of the assets of the company among its creditors, the liquidator shall have regard to directions given by resolution of the creditors or contributories at any general meeting, or by the committee of inspection. But where there is conflict, the directions of the creditors will override the directions of the committee of inspection.

The liquidator shall send to the company's registry an account of his receipts and payments as prescribed by the court or at least twice each year of his tenure and the account will be audited.

The management and the company's remedies during liquidation can only be pursued by the liquidator appointed by the court.

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## Enforcement of estate's rights

- 27** If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Under section 300 and 301 of the CAMA, the creditors may pursue a derivative action to enforce claims in favour of the company, but the fruits of the remedies go to the company. The creditors are only entitled to declaration and injunction.

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## Creditor representation

- 28** What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Where a liquidation order is made by the court and a liquidator is appointed, the court will appoint a committee of inspection from the creditors and contributories or persons holding general powers of attorney from creditors or contributories to inspect the activities of the liquidator. The committee of inspection directs the liquidator on the administration of the company.

The committee of inspection is funded by company funds managed by the liquidator.

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## Insolvency of corporate groups

- 29** In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

A parent company and its subsidiaries are separate legal entities. In insolvency proceedings involving a corporate group, the parent company and its subsidiaries cannot be combined for administrative purposes except there is a special contract between the parent company and its subsidiaries to that effect or where there is fraud.

Except in a special circumstance where the court directs, the assets and liabilities of the parent company and subsidiaries cannot be pooled for distribution purposes.

Assets may not be transferred abroad except where the claims of all the secured creditors have been fully liquidated and the foreign creditor files an application before the court hearing the liquidation petition before the liquidation order is made.

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## Appeals

- 30** What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

A winding-up order is a final decision of the Federal High Court, and under section 241(1)(a) of the Constitution of Nigeria, 1999 (as amended), an appeal shall lie to the Court of Appeal as of right. In relevant cases, the court that made the winding up order may order the appellant to post security in an amount in which the court may think fit before proceeding with the appeal.

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## Claims

- 31** How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Upon advertisement of the petition for liquidation of the company, the creditors would submit their claim by filing an affidavit stating same within 15 days after advertisement of the petition and serve the same on the petitioner. Nevertheless, any delay in the creditor filing its claim that does not amount to a miscarriage of justice is not fatal to the creditor's claim.

Where a creditor cannot prove his claim it will be disallowed and would not be considered in the liquidation order. Under section 456 of the CAMA and section 240 of the Constitution of the Federal Republic of Nigeria, 1999 (as amended), a creditor may appeal against the liquidation order to the court of appeal.

The liquidator may make arrangements, compromise or transfer of claims of the creditor as he or she deems appropriate but same must be disclosed. Claims for contingent or unliquidated amounts cannot be recognised in a liquidation proceeding. The creditor would have to commence an action for the exact amount of the claims to be determined.

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## Modifying creditors' rights

- 32** May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

No.

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## Priority claims

- 33** Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Section 494 provides that labour-related claims rank equally among themselves unless the company's assets are insufficient to meet them, in which case they shall abate in equal proportions. After labour claims are claims of holders of debentures and other secured creditors.

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## Employment-related liabilities in restructurings

- 34** What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

They include all tax deductions, deduction under the pension fund, wages of employees of the company, accrued holiday remuneration and rights under the Workmen Compensation Act.

### Update and trends

The Bankruptcy and Insolvency (Repeal and Re-Enactment) Act is a welcome development. It provides for corporate and individual insolvency, rehabilitation of insolvent debtors, creates the office of supervisor of insolvency and recognises insolvency orders from foreign jurisdictions and appointment of foreign representatives. Like a foreign judgment from Commonwealth countries, insolvency orders from foreign jurisdictions may be registered and enforced in Nigeria.

### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Pension-related claims ranked *pari passu* with labour-related claims.

### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Before the liquidation order is made or a liquidator appointed, the directors of the company are liable for environmental problems and remedy. But once a liquidator has been appointed, he or she will be liable to liabilities and remedy of environmental problems.

### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

No.

### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In reorganisations, the distributions are made by the liquidator in line with the reorganisation plan that the SEC had certified to be fair and equitable and that the court sanctioned.

In liquidation, the liquidator shall manage the business of the company and sell the assets of the company for the purpose of settling the creditor's claims within the time stated in the liquidation order. In distributing the assets, the liquidator must have regard to directions of the resolution of the creditors, committee of inspection and the court.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

In a reorganisation, the purchase of a company of its own shares or distributions to its shareholders contrary to the relevant portion of the Companies and Allied Matters Act is null and void and liable to be annulled.

In liquidation, any transaction relating to property that would, if made or done by or against an individual, be deemed a fraudulent preference in his bankruptcy, shall, if made or done by or against a company, be deemed, in the event of its being wound up, a fraudulent preference of its creditors, and be invalid accordingly. In the same vein, any conveyance or assignment by a company of all its property to trustees for the benefit of all its creditors shall be void.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

No.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

By virtue of section 250 of the CAMA, a person who was not duly appointed as director, but acts as such on behalf of the company, shall not bind the company but be personally liable for his or her actions. In the same vein, under the general grounds for directors' liability, a director shall be personally liable to the company for breach of fiduciary duties and fraud. Section 290 of the CAMA provides that where a director receives a loan, receives advance payment for execution of a contract, with intent to defraud, or fails to apply the money for the purpose it was received, the director will be personally liable to the party from whom the money was received.

In the same vein, under section 502 of the CAMA, if a director before the winding up of a company fails to deliver to the liquidator all the company's property and books in his or her custody, conceals debt due to the company, fraudulently removes any of the company's property, makes any material omission in any statement relating to the affairs of the company, makes a fictitious loss or expense at a meeting with creditors, makes a false representation, or pledges company property that has been obtained on credit in a transaction that is not in the ordinary course of its business, is guilty of an offence and is liable upon conviction to 12 months' imprisonment.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

A parent company can only be liable to liabilities of its subsidiaries or affiliates and vice versa if there is a contract between them to that effect or evidence of fraud.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Once an insider claim is liquidated and can be proved, it may be ranked *pari passu* with unsecured creditors.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Upon making a liquidation order, if there is reasonable proof that a contributory is about to abscond from Nigeria or remove property for the purpose of evading payment of calls, or avoiding examination in respect of company affairs, the court may order the contributory to be arrested and moveable personal property to be seized and kept until a time in which the court may order.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

See question 9 for corporate procedures for liquidation of a corporation.

Under the Bankruptcy Act, where a debtor commits acts of bankruptcy, one or more creditors may file a bankruptcy petition in court

against the debtor for a receiving order against the debtor and his or her assets.

Corporate procedure for liquidation of corporation is an administrative process at the Company Registry while bankruptcy is a judicial proceeding in court.

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#### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Liquidation of a company is concluded upon reaching a compromise between the liquidator and the creditors and contributory and settling the claims of employees, secured and unsecured creditors.

Reorganisation of a company is concluded upon distributions of the assets in accordance with the reorganisation plan sanctioned by the court.

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#### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

See question 8.

Foreign creditors have the same rights as local creditors. They may either file a winding-up petition or file an affidavit in court upon receiving notice of winding-up petition against the company. Their claims will be considered by the court in order of the priority of claims. Also, under the Bankruptcy Act, a Nigerian court shall accord respect to orders from a foreign bankrupt proceeding and a foreign representative appointed by the foreign court.

Monetary judgments and orders from Commonwealth countries are enforceable under the Reciprocal Enforcement of Foreign Judgments Ordinance, Cap 175, 1958. An application for leave to register and enforce the judgment is filed at the division of a High Court where the judgment debtor carries on business within 12 months of the date of delivery of the judgment or when the order was made. The Foreign Judgments (Reciprocal Enforcement) Act, Cap F35, Laws of the Federation of Nigeria, 2004, which provides for a six-year period for registration of foreign judgment, is yet to come into operation because the Minister of Justice has not promulgated an order to that effect.

The New York Convention on the Recognition and Enforcement of Foreign Arbitral Awards, 1958 is applicable in Nigeria. An application for enforcement of foreign awards must be accompanied by the original award and the arbitration agreement or their certified copies.

The recent Bankruptcy Act has adopted some provisions of the UNCITRAL Model Law on Cross-Border Insolvency. The provisions of the Act encourage corroboration between foreign and Nigerian courts in bankruptcy and insolvency proceedings.

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#### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

No.

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#### Cross-border cooperation

#### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Yes. A Nigerian court will implement arrangement to coordinate both local and foreign insolvency proceedings and give effect to the respective orders. The court may apply legal or equitable rules governing the recognition of foreign insolvency orders and assist foreign representatives as long as it is not inconsistent with the provisions of the Bankruptcy Act.

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#### Cross-border insolvency protocols and joint court hearings

#### 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

No. But as the implementation of the Bankruptcy Act takes root, there would be a need for Nigerian courts to hold joint hearings with foreign courts, especially in insolvency cases.

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# Norway

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The most relevant statutes applicable to insolvencies and reorganisations in Norway are the Bankruptcy Act of 1984 and the Satisfaction of Claims Act of 1984. The Bankruptcy Act regulates both judicial debt negotiation proceedings and winding-up proceedings, and mainly provides procedural rules, including criteria for the opening and finalisation of the proceedings. The Satisfaction of Claims Act includes, inter alia, rules on the bankruptcy estate's automatic seizure of the debtor's assets, avoidance (claw-back), how to treat a bankrupt debtor's contracts, as well as rules on creditors' claims for dividend payment and the order of priority for such claims.

The test to determine whether a debtor is insolvent is twofold. First, the debtor has to be illiquid, meaning that the debtor cannot settle debt as it falls due. Second, the total value of the debtor's assets and income is not sufficient to cover the total debt.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Insolvency proceedings shall be opened by the district court where the debtor has its main office or domicile. The court presides over the proceedings opened by that court, and all matters concerning the proceedings are heard by that same court, including ancillary proceedings (eg, avoidance claims or disputes over a creditor's claim). Any appellate proceedings are heard by the regular appellate courts, and, ultimately, the Supreme Court. Besides the trustee's written reports to the court and matters related to the opening and closing of the proceedings, the court is generally not involved unless there is a dispute. Other disputes where the estate is a party are heard in the regular courts and with a different judge than the one presiding over the insolvency proceedings.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Banks, insurance companies and certain other financial institutions, as well as parent companies of such entities, cannot be subject to insolvency proceedings pursuant to the Bankruptcy Act. Insolvency proceedings in such entities are governed by the Guarantee Schemes Act of 6 December 1996 No. 75. The act gives the government the authority to place financial institutions under public administration if:

- they cannot fulfil their obligations as they fall due and they do not have sufficient funds to secure future operations; or
- they are not capable of fulfilling capital adequacy requirements.

If possible, the board of directors will be heard before such actions are taken. If public administration proceedings are opened in a financial institution that is a parent company in a financial group, the other companies in that financial group may also be included in the proceedings.

According to the Satisfaction of Claims Act, the bankruptcy estate has automatic seizure of all the debtor's assets. Exempt from seizure are, for example, certain personal assets and certain monetary contributions the debtor receives while under insolvency proceedings.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There is no specific insolvency legislation for government-owned enterprises and insolvent public enterprises.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No; however specific legislation applies to banks and financial institutions (see question 3).

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

The principal type of security taken on immovable (real) property is a mortgage. Ownership, encumbrances and certain other information about real estate is registered in public national registers, and a mortgage registered in such a register obtains legal protection and extinguishes any argument from a third party claiming to have been in good faith in assuming that the property was not encumbered upon purchase.

Standard forms (in Norwegian) are being used to register mortgages, pledges, etc, and the entire registration process can usually be done in a few days if urgent and handled by a professional. The fees for registering a security interest are very modest, ranging from approximately 500 to 2,600 kroner per asset.

If a creditor has an adequate legal basis for legal enforcement, he or she can deliver a petition for an execution lien in the debtor's property. With a few exceptions, any asset belonging to the debtor may be encumbered with an execution lien. The process of obtaining an execution lien might take months to complete. An execution lien gives the creditor a lien comparable to a pledge or mortgage, including a foundation for requesting a forced sale of the asset in question.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

One cannot generally pledge 'everything that one owns or will own'. It is, however, possible to get a floating charge over certain categories of assets, including 'machinery and plant', 'inventory'/'stock', 'motor vehicles and construction machines' and 'trade receivables'. A floating charge is registered with a fixed maximum amount and includes all the company's assets within that category. Legal protection is obtained by registering the floating charge in the Norwegian Register of Mortgaged Moveable Properties, which will also give protection against alleged

bona fide acquirers. This public register also includes a registration of pledges in specified vehicles.

Pledges in assets that are registered in national registers have to be registered in the relevant register to obtain legal protection. The registration costs are low, and the process of registering the security interest usually takes from a few days to one or two weeks.

As described in question 6, a creditor might be able to attach an execution lien to the debtor's assets. An execution lien may also be effectuated as attachment of earnings.

A vendor's fixed charge or retention of title may be agreed in more or less all types of moveable property, to secure the purchase price and any interest and expenses related to the purchase of that specific asset. If the buyer finances the purchase with a loan that is paid directly from the lender to the seller as settlement of the purchase price, a vendor's fixed charge may also secure such loan. Such security cannot be agreed for assets registered in an assets register or assets that the buyer has a right to resell before they are paid. The latter requirement rules out the possibility of retention of title in inventory/stock. To obtain legal protection, a vendor's fixed charge or retention of title must be agreed between the seller and the buyer for that specific asset before the asset is handed over to the buyer. In a transaction between two professional parties, it is sufficient that such agreement is confirmed in writing without undue delay after the asset was handed over to the buyer. The agreement must state the purchase price and hence the size of the security.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Unsecured creditors can attempt to recover their undisputed claim through a regular debt collection procedure, by attaching an execution lien in the debtor's assets, or by filing for bankruptcy in the debtor, or both. A disputed claim cannot be subject to regular debt collection, but the creditor may seek an execution lien or file for bankruptcy of the debtor, or both. A disputed claim will be heard by either an execution officer or the court before an execution lien is allowed or bankruptcy proceedings opened.

The process of obtaining an execution lien might take months to complete. An execution lien gives the creditor a lien comparable to a pledge or mortgage, including a foundation for requesting a forced sale of the asset in question. The process is usually fairly straightforward and is not expensive.

It will usually take at least one to two months from when the creditor sends notice of a bankruptcy petition to the debtor until bankruptcy proceedings are opened. The difficulty of the process depends on the claim and whether it is disputed by the debtor. An unsecured creditor has to pay a fee, which at the moment is 51,250 kroner, as security for the costs of the bankruptcy proceedings upon delivering the petition to the court.

If an unsecured creditor is worried that the debtor will dispose of assets and reduce the creditor's chances of obtaining coverage for their claim, it may file an injunction petition. The court then decides whether or not to grant the petition and issue an order preventing the debtor from, for example, disposing of assets.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A debtor wanting to commence a voluntary liquidation case must be insolvent. The debtor must deliver a written petition for bankruptcy to the court, supported by a set minimum of documentation.

The court rarely denies a petition for voluntary liquidation.

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

A bankruptcy petition from one or more creditors must be in writing. The petitioner must provide documentation for the claim and its foundation. If the court finds that the claim is well founded and sufficiently

documented, or if the claim is undisputed and the debtor cannot pay, the court will grant the petition and open bankruptcy proceedings in the debtor. If the claim is disputed, or if the debtor claims it is not insolvent, the court will hear the parties before deciding on whether or not to open proceedings.

If the court decides to grant the petition, the debtor is taken under bankruptcy proceedings. If the court denies the petition, proceedings are not opened and the debtor may continue its operations as usual. If the court has denied the petition because it found the creditor's claim unfounded, the decision cannot be used by the debtor as evidence that the creditor has no claim. Hence, the creditor may initiate court proceedings before a regular court to determine whether their claim is valid. If the court decides that the claim is valid and the debtor continues not to pay, the creditor may thereafter deliver a new petition for bankruptcy in the debtor.

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### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

A debtor who cannot meet its financial obligations as they fall due may file for a formal financial reorganisation/debt negotiation proceedings. A voluntary process can only be successful if the reorganisation plan is accepted by all of the creditors.

The petition to the court to open proceedings must be made in writing, and must fulfil certain contents and documentation requirements set out by the Bankruptcy Act.

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### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Creditors cannot commence an involuntary reorganisation of a Norwegian debtor. However, a debtor that cannot meet its obligations as they fall due may itself file for a 'compulsory' debt negotiation proceeding, under which creditors/debt may be crammed down, subject to certain rules.

The petition must fulfil the same criteria as in a voluntary process (see question 11).

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

The board of directors in a limited liability company must act promptly if the company's equity is considered insufficient compared with the size and risk of the business operations, or if the company's equity is less than half of the share capital. Such actions include measures to improve the company's financial situation, convene a shareholders' meeting to discuss the situation and ultimately to file for bankruptcy proceedings if it is unlikely that the financial difficulties can be resolved in the immediate future. Failing to meet its obligation to act, and for the board of directors to carry on business while the company is insolvent may result in penal liability or economic responsibility for the directors, or both.

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

In a formal reorganisation process in Norway, either voluntary or involuntary, the debtor retains legal powers over its assets, and the company's board of directors maintains responsibility for the ongoing business. The debtor and its operations are, however, supervised by an administrator and a debt negotiations committee, both appointed by

the court. The debtor cannot renew or obtain new debt, pledge assets or sell or lease out its real property, business premises or any asset of significant value without the consent of the administrator and debt negotiations committee.

Creditors who supply goods or services after the filing will not be given any special treatment.

The members of the court-appointed debt negotiations committee are usually representatives for the largest creditors.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

The opening of an insolvency proceeding triggers an automatic stay on enforcement proceedings against the debtor, including a creditor's attempt to attach an execution lien in any of the debtor's assets. The stay lasts six months from when the proceedings are opened.

After a petition for judicial debt negotiation proceedings has been filed, there is a three-month automatic stay of any petitions for winding-up proceedings related to debt incurred prior to the opening of the judicial debt negotiation proceedings. The stay may be prolonged at the discretion of the court upon a motion from the debtor. If compulsory judicial debt negotiation proceedings are opened, the automatic stay lasts throughout the proceedings.

The automatic stay is, however, not effective against a petition for winding-up proceedings filed by at least three creditors with voting rights whose total claims in sum represent at least two-fifths of all claims entitled to dividend payment, even though the debt arose prior to the filing of the petition.

If the debtor at the time of the opening of liquidation proceedings is the claimant in a legal proceeding, the case is automatically stopped by the court. If the debtor is the defendant, however, the claimant may choose to include the bankruptcy estate as a defendant in the legal proceeding.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

A debtor in liquidation may not obtain secured or unsecured loans or credit. A debtor in a formal reorganisation (debt negotiation proceedings) may only obtain loans or credit if accepted by the debt negotiations committee.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

The general rule is that a creditor may exercise its right to set-off its claim after insolvency proceedings have been opened against the debtor, if the general terms of set-off are fulfilled and a set-off, therefore, was possible before proceedings were opened. However, if the debtor's claim against the creditor fell due before proceedings were opened, and the creditor's claim does not fall due until after proceedings were opened, the creditor is permanently deprived of the right to set-off.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

In judicial debt negotiation proceedings, the sale of specific assets or the entire business of the debtor are generally subject to the same

rules as a company that is not in any insolvency proceeding; however the debtor is supervised by a debt negotiations committee, which shall approve the sale of any assets of significant value. If a compulsory judicial debt negotiation proceeding is successful, any encumbrances that supersede the assumed value of the encumbered assets cease to exist.

In liquidation proceedings, the business may be sold free and clear of debt (see the Bankruptcy Act, section 117a). In such a sale, encumbrances that supersede the value of any asset sold by the bankruptcy estate may be eradicated if they are sold together with other assets, or as part of the business operations, subject to certain further statutory conditions. This provision is, however, quite narrow and hardly ever used in practice, meaning that a bankruptcy estate usually must respect and deal with any pledgees.

There is no practice of 'stalking horse' bids in sale procedures in Norwegian insolvency proceedings. Credit bidding in sales is not practiced in Norwegian insolvency proceedings, and an unsecured creditor cannot purchase assets from the insolvent debtor by reducing the amount of its claim against the debtor.

Any encumbered asset of the debtor may be transferred to the pledgee holding security in that asset, in exchange for the pledgee reducing its claim against the debtor accordingly (see the Bankruptcy Act, section 117c).

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

In insolvency proceedings, IP agreements are treated as most of the debtor's contracts: the estate has a right to enter into the contract as a party. This means that the IP licensor or owner may not terminate the debtor's right to use it if the estate enters into the contract as a party. If the estate does not want to become a party to the contract, however, the debtor's contractual party may terminate the agreement.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

An insolvency estate in Norway will have the same rights and obligations as the debtor, and in general, the estate has the opportunity to use or transfer personal information or customer data collected by the debtor to the same extent as the debtor.

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### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

A debtor undergoing judicial debt negotiation proceedings may not reject or disclaim an unfavourable contract merely because of the opening of proceedings; the debtor's contracts remain unchanged after debt negotiation proceedings are opened. However, when liquidation proceedings are opened, the bankruptcy estate may choose to enter into or to disregard any of the debtor's contracts. As for tenancy agreements and employment contracts, the bankruptcy estate automatically becomes a party and must explicitly declare to the contractual parties within four and three weeks, respectively, if it does not want to remain a party to either contract.

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**Arbitration processes in insolvency cases**

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

If arbitration is used in insolvency proceedings, it is never used in the actual insolvency proceeding, but, for example, in an ancillary proceeding and/or in a dispute concerning a contract of the debtor with an arbitration clause.

If the debtor was party to an arbitration proceeding when the insolvency proceedings were opened, the estate may choose to continue those proceedings. A bankruptcy estate may agree to arbitrate a case where the estate is the plaintiff or defendant; however, it will most likely never do so because it is far more expensive than having the case brought before a regular court.

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**Successful reorganisations**

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

In a voluntary debt negotiation proceeding, the creditors have to be treated equally. There are no other mandatory features; however, the plan must be accepted by all creditors.

In a compulsory debt negotiation proceeding where the debtor suggests a compulsory composition, the minority voters are crammed down by the majority voters. The plan must provide a minimum dividend payment of 25 per cent to all unsecured creditors with claims not ranking in priority, and the reorganisation plan requires a majority both in number of creditors and of the total amount of all claims filed to be binding on all creditors (ie, 'double majority').

The main requirements for reaching a double majority in a compulsory composition are (the numbers referring to creditors and claims that are granted voting rights):

- if the dividend payment is at least 50 per cent, the plan must be accepted by at least three-fifths of the creditors holding at least three-fifths of the total debt; or
- if the dividend payment is less than 50 per cent (but not below 25 per cent), the plan must be accepted by at least three-quarters of the creditors holding at least three-quarters of the total debt.

Claims ranking in priority shall be paid in full, and will, therefore, not entitle the respective creditors the right to vote. Nor will secured claims give grounds for voting rights, to the extent that they would have received payment if the secured assets were to be sold or realised. Finally, closely related parties to the debtor do not have the right to vote.

A reorganisation plan will in itself not release non-debtor parties from liability.

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**Expedited reorganisations**

- 24 Do procedures exist for expedited reorganisations?**

No.

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**Unsuccessful reorganisations**

- 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

A voluntary debt negotiation plan cannot be carried out unless it is approved by each of the debtor's creditors.

A proposed compulsory plan is defeated if the voting requirements (see question 23) are not met. Further, the court may in certain situations decide not to accept the plan, for instance, if the procedure has not been carried out in accordance with the law or if the plan does not treat the creditors equally and the creditors have not agreed to differential treatment. Other reasons the court may have for not accepting a plan include that it would be unreasonable or that it is considered likely that the debtor will not be able to fulfil the plan.

The court may decide that the debtor's fulfilment of the plan shall be supervised, usually by one or more members of the debt negotiations committee. If a debtor is subject to supervision and severely or repeatedly acts against its duties, the court shall open liquidation proceedings against the debtor if petitioned by the supervisor or supervisors, and if it is not clear that the debtor nevertheless will be able to fulfil the plan. If a non-supervised debtor fails to adhere to a plan, there are no automatic consequences; however the creditors may initiate (new) debt recovery proceedings.

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**Insolvency processes**

- 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

In compulsory judicial debt negotiation proceedings, the debt negotiations committee shall hold a meeting for the creditors. The meeting should be held no earlier than four weeks after proceedings are opened, and shall be held no later than eight weeks after proceedings are opened.

The court-appointed administrator in a bankruptcy case shall inform all known creditors of the bankruptcy proceedings.

In liquidation proceedings, the court usually schedules a creditors' meeting within two to four weeks after proceedings are opened. In that meeting, the court-appointed administrator delivers a report regarding the status and findings of the proceedings, which is also made available to all creditors. Unless there are special circumstances that necessitate a second or more creditor meetings, no further such meetings are held. The date and time of the first creditor meeting is stated in the court's decision to open proceedings.

If the proceedings last longer than a year, or several years, the court-appointed administrator and creditors' committee shall each year prepare an annual report to the court. The report is also made available to all creditors.

A creditor may ask for, but has no specific right to receive, further information regarding the estate and the proceedings. A request for transparency is considered and decided on in each separate case.

Creditors may pursue claims against third parties after the insolvency proceedings are finalised. See question 27.

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**Enforcement of estate's rights**

- 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

If the insolvency administrator has no assets to pursue a claim, creditors may pursue claims against third parties after the insolvency proceedings are finalised, but do not subrogate the estate's position; each creditor must consider whether it has grounds to pursue a claim individually or in cooperation with other creditors. Any creditor may, for whatever reason, decide to fund the estate's pursuit of a claim. Such funding will be pursuant to an agreement between the estate and the creditor. If the outcome concerns the body of creditors, the funding creditor will not be given preferential treatment other than, usually, receiving a cost refund if the outcome of the pursuit is positive.

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**Creditor representation**

- 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

When liquidation proceedings are opened, the court often, but not always, appoints one or more individuals to form a creditors' committee. The committee more or less functions as a 'board of directors' for the estate, with the trustee as chairman and other members as directors. The committee makes decisions for the estate, for example, deciding when and how to realise assets, whether or not to pursue claims, and is responsible for testing claims filed in the estate before carrying out any distribution to the creditors.

Usually the trustee suggests to the court one or more creditor representatives to appoint as members of the creditors' committee. A creditor who is interested in being on the committee may notify the trustee. In larger cases, the committee usually has at least two creditor representatives as well as a representative for the employees.

The creditors' committee's members are paid from the estate provided that the estate has available means. In the smaller estates, the members of the creditors' committee might not receive any remuneration. The committee may retain advisers; however, it can only do so if it is pro bono or if there are sufficient funds in the estate.

A creditors' committee in judicial debt negotiation proceedings have more of a supervisory function (see question 14).

### Insolvency of corporate groups

**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

In insolvency proceedings involving a corporate group, the proceedings by the parent and its subsidiaries are often combined in the sense that the same administrator is appointed for the separate proceedings. However, the decision of whom to appoint as trustee is subject to the discretion of the court that opens the proceedings, and there is no automatic appointment of the same trustee for the insolvency proceedings of all companies in a group.

The assets and liabilities of companies in the same company group and under insolvency proceedings may not be pooled for distribution purposes; each estate handles its own assets, and distribution/dividend payment is done from each estate.

Norwegian law does not allow for a mere transfer of assets from an administration in Norway to an administration in another country, unless it is a regular sale/purchase or in accordance with another mutual agreement.

### Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

All court orders may be appealed within a month of its passing. An appellant has an automatic right of appeal, and does not need to obtain permission to do so. The appellant must, however, have a legal interest in the matter. There is no requirement to post security to proceed with an appeal; however, the appellant must pay a court fee. The size of the court fee varies and depends on which type of decision is appealed, whether a court hearing is held and for how many days, etc.

### Claims

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

When the court opens insolvency proceedings, it sets a time limit for filing claims in the estate. The time limit shall be within three and six weeks from when the opening of proceedings was announced in The Bronnoysund Register Centre. The time limit is, however, not preclusive, and claims filed after the time limit has expired, but before the proceedings are finalised, will be registered in the estate.

Claims filed in the estate will only be tested if there are sufficient funds in the estate to give distribution to the class of claims in which the respective claims belong. The trustee tests the claims by assessing documentation provided by the creditor, and decides whether or not to recommend to the creditors' committee to allow the claim. If a claim is disallowed, and the creditor and estate do not reach an amicable agreement, the trustee informs the court of the matter, and the court sets

a deadline of three weeks for the creditor to take legal action in order for the court to decide on the matter. If the creditor does not take legal action within the deadline, the claim will be treated in accordance with the trustee's recommendation without any possibility of appeal.

A claim filed in the estate may be transferred, and it is sufficient to give notice to the estate of such a transfer.

Contingent claims may be recognised and recommended. However, such claims will only receive dividend payment to the extent that the condition has occurred. If the condition has not occurred, the dividend payment for the contingent claim shall be preserved by the trustee on account and only paid out to the creditor if and when the condition occurs.

A claim acquired at a discount may be enforced for its full face value.

Interest accrued after insolvency proceedings were opened may be filed as a dividend claim in the estate; however, it will rank last in priority.

### Modifying creditors' rights

**32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

If the trustee finds that the creditor has filed its claim in a higher priority than it should have, but the creditor disagrees, the trustee shall report the matter to the court (see question 31). If the creditor takes legal action within the three-week deadline set by the court, the court may change the priority of the creditor's claim if the court agrees with the trustee. If the creditor does not take legal action within the deadline, the claim and its priority will be treated in accordance with the trustee's recommendation.

### Priority claims

**33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Employees' claims for unpaid wages, with certain limitations, rank first in priority. With mainly the same limitations and up to a certain maximum amount, outstanding wages will, in the event of a bankruptcy, be covered by the Norwegian Wages Guarantee Fund. The Wages Guarantee Fund then subrogates the employee's claim and becomes a creditor in the estate for the same amount that was paid by the Fund to the employee.

Certain tax and VAT claims rank second in priority. Remaining claims have no priority, except for interest accrued after the bankruptcy proceedings were opened and certain other claims, which rank last in priority.

Creditors with security for their claims will have priority to the assets in which they have security. Any part of a secured creditor's claim that is not covered by the realisation of such assets will be an unsecured claim in the estate and thus have no priority.

Claims that have arisen after the opening of bankruptcy proceedings (eg, payment for a service requested by the estate) shall be covered before any creditors with dividend claims receive any distribution.

A bankruptcy (liquidation) estate has a statutory lien in all pledged assets belonging to the debtor and assets pledged as security by third parties for the debtor's liabilities. The lien is 5 per cent of the sales proceeds of each pledged asset, limited to a maximum amount for each asset (717,500 kroner as of September 2016). The lien has priority over all other liens and security interests. The proceeds from the lien may only be used to cover the estate's necessary administration costs and expenses, and only if the estate does not have other funds to cover such costs.

### Employment-related liabilities in restructurings

**34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

In a liquidation proceeding, the bankruptcy estate automatically becomes a party to all employment contracts, and must expressly declare to the employees within three weeks if it does not want to be a party to the respective contract. There are no specific employee claims

### Update and trends

There have been written hearings and opinions on whether Norway should implement the EC Insolvency Regulation, but there is still no such proposal from legislators. The Regulation will likely not be ratified in Norway for several years (if, indeed, at all). However, in April 2016, the Ministry of Justice and Public Security published a legislative proposal to add a Chapter to the Bankruptcy Act, with new provisions on cross-border insolvency matters. The Chapter includes provisions on both territorial and factual jurisdiction, choice of law rules, as well as recognition of foreign insolvency proceedings and the impact foreign proceedings shall have in Norway. Some of these legal principles appear to resemble certain provisions of the EC Insolvency Regulation. An amending Act complying with the legislative proposal was enacted

by the Norwegian parliament in June 2016, but has not yet entered into force.

The judicial restructuring scheme in Norway is under review, subject to a mandate given by the Ministry of Justice to Judge Leif Villars-Dahl with the Oslo Court of Probate and Enforcement. His mandate included, inter alia, to evaluate whether the current rules should be amended to facilitate a more flexible restructuring scheme with the aim of saving more businesses and preserving more jobs. Judge Villars-Dahl submitted his evaluation report on 1 March 2016. The Ministry of Justice appointed a group of three lawyers and one economist to support him in his work: attorney Knut Ro, attorney Ståle Gjengset, attorney Stine D Sneringdalen and Professor Nils-Henrik von der Fehr.

that arise where employees are terminated during a restructuring or liquidation.

The procedures for termination in a restructuring are the same as outside a restructuring. The rules of terminating the employment contracts are more or less the same as outside a liquidation proceeding, and the estate must issue termination notices to each and every one of the employees.

### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Pension-related claims against an employer in insolvency proceedings are subject to more or less the same rules as claims for wages (see question 33). Pension-related claims rank first in priority, with certain limitations, and will to an extent be covered by the Norwegian Wages Guarantee Fund.

### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Any environmental problems that arose prior to the opening of insolvency proceedings are usually left with the debtor, and no liabilities are imposed on the insolvency administrator or estate. There could, however, be grounds for liability for the debtor's officers and directors. If environmental problems are caused by the bankruptcy estate, the estate and/or the insolvency administrator could be held liable, depending on the circumstances.

### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Liabilities of personal debtors (ie, debtors that are not limited liability companies or other structures with limited liability) survive an insolvency or a reorganisation. This entails that the debtor's debt and liabilities do not go away when the proceedings are finalised. The debt may, however, be reduced or waived by the creditors as part of the process, or the debtor and its insolvency estate may carry out a compulsory composition, forcing a reduction of debt.

### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Distributions to creditors may be carried out both during the proceedings and after the proceedings have been finalised. The main prerequisite for distributing dividend payments to creditors during the proceedings is that there are obviously sufficient funds in the estate to make such payment. Prior to any distribution, the claims are tested (see question 28).

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

There are several provisions regulating different kinds of transactions that may be annulled (eg, transactions considered to be extraordinary payments, gifts, security for old debt and certain cases of set-off). In general, the transaction in question must have been performed within three months prior to the date on which the court received the bankruptcy petition (for gift transactions, the general time limit is one year). However, older transactions may also be annulled if the beneficiary and the debtor were closely related parties (applying a two-year time limit), or if the beneficiary has not acted in good faith with regard to the poor economic state of the debtor and the unfairness of the transaction (applying a more subjective element of assessment and a 10-year time limit).

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The estate has one year from the opening of bankruptcy proceedings to forward an annulment claim. Such claims may only be attacked by a bankruptcy (liquidation) estate or by the debt negotiations committee in compulsory debt negotiation proceedings.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Corporate officers and directors may be held liable for their corporation's obligations, but only if they can be held accountable for why the company has built up those obligations.

The board of directors has certain duties when the company is experiencing financial difficulty, and failure to comply with such duties may lead to the directors being held liable for damages or criminally liable. For instance, they shall ensure that the company's creditors are treated fairly and equally, and that the company does not incur any debt that it cannot pay unless the creditor is familiar with, or informed of, the company's financial situation and the risks involved with providing credit.

Furthermore, the directors must act promptly if the company's equity is considered insufficient compared with the size and risk of the business operations, or if the company's equity is less than half of the share capital (see question 13).

If the bankruptcy trustee finds that corporate officers/directors are guilty of criminal violations (typically a lack of accounting duties or embezzlement) or unfit to run a business, the trustee may suggest to the court that those responsible are put in 'bankruptcy quarantine'. Such quarantine lasts for two years, and entails that the quarantined person cannot establish a new company or be a corporate officer or director in any company for the duration of the quarantine period.

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**Groups of companies**
**42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

A parent company may in certain situations be held responsible for the liabilities of subsidiaries, and especially in situations where it is the board of directors of the parent company that in reality has acted as the board of directors of the subsidiary, or where the boards of directors have worked so closely together that the directors can be held mutually liable.

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**Insider claims**
**43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

In general, there are no restrictions on such claims.

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**Creditors' enforcement**
**44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

Besides a bankruptcy estate's automatic seizure of assets, there are no processes by which some or all of the assets of a business may be seized outside of court proceedings.

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**Corporate procedures**
**45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

Forced liquidation or dissolution proceedings follow the procedural rules of a winding-up proceeding and are governed by the Bankruptcy Act. The law differentiates between forced dissolution and forced liquidation, as the conditions for the opening of the two proceedings are different.

The court may take charge of a dissolution process if the company has reported to the National Register of Business Enterprises that it is in the process of a regular dissolution but has not managed to complete the dissolution process within a year from delivering the first notification. The court may also take charge of a dissolution process if this is requested by shareholders representing at least one-fifth of the total shares in the company.

A company may be subject to a forced liquidation process if it has failed to fulfil certain legal requirements, including those related to the composition of the board of directors, the appointment of an authorised public auditor and the reporting of the company's annual accounts to the Register of Company Accounts.

Insolvency is not a precondition for the opening of forced dissolution or liquidation. The business may even be solvent and ongoing and still be subject to proceedings, as the conditions to open such

proceedings are objective and absolute. Nevertheless, most of these cases result in liquidation of the company, since the process of returning the company to its shareholders is often complex, time-consuming and expensive.

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**Conclusion of case**
**46 How are liquidation and reorganisation cases formally concluded?**

Judicial debt negotiation proceedings are a 'make or break' situation for a company, and are finalised either by a successful reorganisation plan being carried out, or by ending in liquidation proceedings. The conclusion is either way formally decided by the court.

Liquidation proceedings are formally concluded by a court decision.

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**International cases**
**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

An insolvency proceeding in another country is in general not recognised by Norwegian courts unless that country has a mutual agreement with Norway. A Supreme Court decision from 2013, however, implies that although a foreign insolvency proceeding does not impose a stay on creditors' debt recovery proceedings against any assets the foreign debtor has in Norway, a foreign bankruptcy estate will be acknowledged in Norwegian courts as a representative for the common interests of the debtor's creditors. In other words, the foreign bankruptcy estate might, according to the decision, be treated equal to and have the same debt recovery possibilities as any other unsecured foreign creditor of the debtor.

Foreign creditors in a Norwegian insolvency proceeding are generally not treated differently from national creditors.

Foreign judgments or orders are recognised to the extent that they are subject to either the Lugano Convention or another convention or agreement between Norway and that state. In addition to the Lugano Convention, Norway is a party to the Nordic Convention on Bankruptcy, which, inter alia, regulates cross-border insolvencies within Norway and the other member states; Denmark, Sweden, Finland and Iceland. Further, the Nordic Convention has rules on recognition and enforcement as well as choice of law in various situations.

The UNCITRAL Model Law on Cross-Border Insolvency has not been adopted by Norway. There are, however, legislative changes in motion that to a large extent will implement elements from the UNCITRAL Model Law.




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**COMI****48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

A company's COMI is generally where the company has its registered main office/business address. However, if the company has its actual centre of business elsewhere, the COMI may be decided to be where the actual business is performed, and not only where it has its registered address.

**Cross-border cooperation****49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

Norway does provide for recognition of foreign insolvency proceedings where there is a mutual agreement in place between the states (see question 47). Domestic and foreign courts rarely cooperate.

Norwegian courts have refused to recognise foreign proceedings. For instance, the Supreme Court ruled in a 2013 decision that acknowledgement of insolvency proceedings in another state must primarily be in accordance with mutual agreements or legislation.

**Cross-border insolvency protocols and joint court hearings****50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

No.

# Peru

Rafael Corzo de la Colina, Renzo Agurto Isla and Lisbeth Benavides Kolind-Hansen  
Miranda & Amado Abogados

## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

Insolvencies and reorganisations are regulated by Law No. 27809 (the Insolvency Law). The Insolvency Law does not provide a particular definition for 'insolvency'. However, it establishes different requirements in order to commence voluntary or involuntary insolvency proceedings, which could be assimilated to the criteria applicable to determine if a debtor is insolvent.

The Insolvency Law regulates two types of proceedings: the ordinary insolvency proceeding (ordinary proceeding) and the preventive insolvency proceeding (preventive proceeding).

To access a voluntary ordinary proceeding, the debtor must prove –among other things– that more than one-third of its outstanding liabilities have been due for more than 30 calendar days or, alternatively, its accumulated losses minus its retained earnings exceed one-third of its paid-in capital. A debtor shall only request its liquidation if its accumulated losses minus its retained earnings exceed its paid-in capital. For a creditor to initiate an involuntary ordinary proceeding, it must prove that its outstanding credit exceeds 50 tax units (approximately US\$61,000) and that such an amount has been due for more than 30 calendar days.

In the case of the preventive proceeding (which according to the Insolvency Law is always a voluntary proceeding), the debtor must prove, among other aspects, that it is not in any of the situations described as requirements to access to a voluntary ordinary proceeding.

Also, in August 2015 the Insolvency Law was amended by means of Legislative Decree No. 1189. The amendments introduced by Legislative Decree No. 1189 have been in force from 20 October 2015; however, a disposition regarding the term of liquidations as a going concern came into force on 22 August 2015 (ie, on the date following that of the publication of the Legislative Decree in the official gazette). In addition, in August 2016, Law No. 30502 was enacted in order to authorise extraordinary extensions to the term set in the Insolvency Law for liquidations as a going concern.

Finally, it should be considered that special insolvency legislation has been enacted in order to allow the restructuring of certain professional football clubs (Law No. 29862 and Law No. 30064).

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Peru has had an administrative proceedings insolvency system since 1992. The insolvency authority, the National Institute for the Defence of Competition and the Protection of Intellectual Property (INDECOP), is a public technical specialised agency of the executive branch, who through its Insolvency Commission (the Commission) deals solely with insolvency proceedings. INDECOP's second instance (which deals with appeals to the Commission's decisions) is the INDECOP's Tribunal (specifically, the Chamber Specialising in Insolvency Proceedings of the INDECOP's Tribunal).

Although courts do not participate directly in the insolvency proceedings, they are involved in aspects associated to the proceedings such as the following:

- courts are in charge of the proceedings for the avoidance of certain agreements entered into during the suspect and avoidance periods (see question 39);
- courts are competent to rule in contentious-administrative judicial review proceedings in which INDECOP's Tribunal decisions are challenged;
- courts are in charge of criminal law proceedings related to insolvency-related crimes; and
- courts are competent to declare the bankruptcy of the debtor. Under the Insolvency Law, the term 'bankruptcy' is used only to describe the situation in which, after a liquidation proceeding, some creditors remain unpaid even though no assets remain.

The Insolvency Law contains specific provisions in order to restrain actions of creditors or debtors through courts (particularly through the commencement of constitutional proceedings such as the *amparo* proceeding) related to aspects that are exclusively in charge of INDECOP.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The following entities are excluded from the insolvency proceedings that are regulated in the Insolvency Law:

- entities that are part of the Peruvian state structure, such as public sector entities;
- private pension funds (Supreme Decree No. 054-97-EF);
- banks, financial institutions, insurance companies and other entities that are regulated by the General Law of the Financial and Insurance Systems (Law No. 26702); and
- certain special purpose vehicles or 'autonomous property' such as trusts, mutual funds and investments funds. Descendants' estates and community property are under the scope of the Insolvency Law.

Also, individuals that do not carry out business activities are excluded from the insolvency proceedings regulated in the Insolvency Law.

Note that if an insolvent debtor has granted a guarantee related to a particular asset (rights in rem such as a pledge or mortgage) in favour of a third-party obligation, such a secured party can enforce its rights according to the respective agreement terms, independently of the fact that the guarantor (the insolvent debtor) is subject to an insolvency proceeding (the automatic stay will not be opposable against such secured party). Goods that are considered as unattachable property by the Civil Procedural Code (eg, state property considered of public use or public domain) will be exempt from creditor's claims.

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

Government-owned enterprises are not subject to the Insolvency Law. Pursuant to the FONAFE Guidelines approved by FONAFE's Board of Directors Resolution No. 001-2013/006-FONAFE (as amended), the

liquidation proceeding of government-owned enterprises is carried out by a liquidator appointed by the shareholders' meeting and according to a liquidation plan approved by the same shareholders' meeting. To the extent that the above-mentioned guidelines do not regulate all aspects of the liquidation proceeding of government-owned enterprises, the specific proceeding to be followed (and the remedies available to the creditors) will have to be determined on a case-by-case basis and based on the specific resolutions adopted by the shareholders' meeting and under some FONAFE decisions.

Notwithstanding the above, there are currently certain state-owned enterprises that are excluded from the scope of FONAFE, and that would therefore be subject to the insolvency regime applicable to all corporations under the Insolvency Law.

#### Protection for large financial institutions

##### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No. However, it should be noted that the Peruvian banking regulatory framework does contain specific prudential rules that apply to holding companies of banks and insurance companies, which include consolidated capital requirements and consolidated risk management controls and supervision.

#### Secured lending and credit (immoveables)

##### 6 What principal types of security are taken on immoveable (real) property?

The principal securities over immoveable property are mortgages. The creation of a mortgage requires the execution of a public deed before a public notary and its registry before the Public Registry.

Immoveable property can also be transferred to trusts under the provisions of the General Law of the Financial and Insurance Systems (also created by means of public deed and subject to registration before the Public Registry). The trust estate is autonomous and independent and is not subject to the insolvency risk of any of the parties. However, trusts can be put under scrutiny pursuant to the suspect and avoidance periods regulated under the Insolvency Law (see question 39). Moreover, pursuant to the General Law of the Financial and Insurance Systems, the transfer of assets to a trust can be annulled when such transfer is made incurring in creditors' fraud. The action for this annulment prescribes after six months following the publication of the creation of the trust in the official gazette, *El Peruano*.

#### Secured lending and credit (moveables)

##### 7 What principal types of security are taken on moveable (personal) property?

The principal security devices relating to moveable property are asset pledges and trusts (under the same principles explained in question 6). Asset pledges are opposable to third parties only if a public instrument has been duly filed and registered before the Public Registry.

#### Unsecured credit

##### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Prior to the initiation of an insolvency proceeding, unsecured creditors can initiate judicial proceedings to obtain payment of their credits. Seizures and attachments, including pre-judgment attachments, are available in all types of judicial proceedings initiated for such a purpose.

If a seizure or attachment is granted by a court, in practice, the creditor will have similar rights (priority) to those that are granted to creditors that have guarantees over immoveable or moveable property of the debtor.

The difficulties and timescales of the judicial processes depend on the complexity of the claim. In general, judicial processes are time-consuming, however, the processes might be quicker if the creditor has an executory instrument.

As mentioned in our answer to question 15, as of the 'bar date' (ie, the date when the beginning of the insolvency proceeding is published in the official gazette), all obligations of the debtor become temporarily

unenforceable and, thus, all execution proceedings for collection as well as injunctions (related to pre-publication claims) against the debtor's estate will be stayed.

There are no special proceedings applicable to foreign creditors.

#### Voluntary liquidations

##### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Voluntary and involuntary liquidations and reorganisations can only be carried out under the framework of an ordinary proceeding. In order to initiate a voluntary proceeding, the debtor must comply with the following patrimonial requirements: more than one-third of its outstanding liabilities must have been due for more than 30 calendar days or, alternatively, its accumulated losses minus its retained earnings exceed one-third of its paid-in capital. However, if its accumulated losses minus its retained earnings exceed its paid-in capital, the debtor can only request its liquidation.

Formal requirements for the commencement of the proceeding include the presentation of a copy of the shareholders' meeting minutes with the shareholders' authorisation for the commencement of the proceeding and a copy of the last two years' financial statements. Currently, if the outstanding liabilities exceed 100 tax units (approximately US\$120,000), the financial statements shall be audited.

In addition, if the debtor is an individual, decedent's estate or community property (*sociedad conyugal*), it will need to prove that more than 50 per cent of its income comes directly from the debtor's economic activity or more than two-thirds of its liabilities were originated by such a debtor.

Even with the above-mentioned requirements, the creditors' meeting can decide to change a reorganisation to a liquidation and vice versa (certain special rules will apply).

It is important to distinguish between the effects of the commencement of the proceeding by the debtor (the filing of a petition before INDECOPI for the commencement of an ordinary proceeding) from the effects produced as of the 'bar date' (ie, the date when the beginning of the insolvency proceeding is published in the official gazette). The effect of the filing of the petition is that such a date will determine the date that will be used to calculate the suspect and avoidance period terms (see question 39). The proceeding to finally obtain a formal decision of INDECOPI that declares the insolvency of the debtor and the corresponding publication of such a decision in the official gazette (the bar date) could take between three and six months.

With the release of the publication, an automatic stay is imposed (see question 15).

Any claim originated before the bar date will be considered a pre-publication claim. Only pre-publication claims are subject to the Insolvency Law rules, INDECOPI's venue and the terms and conditions of the reorganisation or liquidation plan. In order to participate in the creditors' meeting, creditors must file a proof of claim before INDECOPI within 30 business days from the bar date. Only those creditors that are allowed by INDECOPI can participate in the creditors' meeting. Allowed claims will be paid before non-allowed claims either in a reorganisation or liquidation.

In the case of voluntary or involuntary liquidations, the creditors' meeting will mainly designate a liquidator (who must be a liquidator registered before INDECOPI), approve a liquidation plan and decide if the debtor can carry out business during the liquidation as a going concern (the maximum term for this type of liquidation is one year, extendable for one additional year). Also, pursuant to Law No. 30502, enacted in August 2016, the creditors' meeting is allowed to grant an extraordinary extension of one additional year to the maximum term for liquidations as going concerns; and the executive branch of the government, at the request of the creditors' meeting and with a prior report from INDECOPI, is allowed to prolong such extraordinary extension for one additional year, by means of a Supreme Decree.

#### Involuntary liquidations

##### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

For general requirements and effects, see question 9.

For a creditor to initiate an involuntary ordinary proceeding, it must prove that its outstanding credit exceeds 50 tax units (approximately

US\$61,000) and that such amount has been due for more than 30 calendar days. Although the Insolvency Law used to ban secured creditors from initiating insolvency proceedings, this limitation was eliminated with the latest amendment that was made to the Insolvency Law. This amendment also now allows creditors to initiate an insolvency proceeding against debtors that have already initiated a liquidation under the General Corporations Law (in which case the liquidation under the General Corporations Law will be stayed during the duration of the insolvency proceeding).

Note that there used to be a particular type of involuntary liquidation that was initiated under the rules of the Civil Procedural Code and that was recently abolished by Law No. 30201 (published on 28 May 2014). According to this new law, if, in an executory proceeding, the debtor does not offer assets free of liens or encumbrances to its unsecured creditor, the court can register such debtor in a defaulting debtor registry until the credit originating such executory proceeding is paid in full (previously, according to the abolished regulation the court had to declare the debtor's insolvency).

Under certain circumstances (eg, when the creditors' meeting fails to approve a reorganisation plan within the time limits established in the Insolvency Law), the Commission can declare the liquidation of the debtor. However, the creditors' meeting is allowed to revert such decision and resolve to submit the debtor to a reorganisation process.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

##### Ordinary proceeding

For general requirements and effects, see question 9.

According to the Insolvency Law, the decision to reorganise a debtor will be exclusively in hands of the creditors' meeting. The creditors' meeting shall approve a reorganisation plan within 60 business days from its decision to reorganise the debtor. The decision to reorganise the debtor and the approval of a reorganisation plan must be approved by more than 66.6 per cent of the allowed claims (in the first call of the creditors' meeting) or more than 66.6 per cent of the allowed claims attending the creditors' meeting (in the second call). Whenever the allowed related creditors amount to more than 50 per cent of allowed claims, any decisions pertaining to either the approval of the reorganisation or liquidation of the debtor or the approval of the liquidation plan, reorganisation plan (and its amendments) and debt financing arrangements (in the case of preventive proceedings) must be voted separately by the related party creditors and the non-related creditors. In these cases, such decisions will be deemed approved if the aforementioned majorities are met in both the related and non-related creditors' meetings.

All allowed creditors (whether secured or not) participate in the creditors' meeting on an equal footing as the participation of each creditor is determined not by their payment priority order, but by the percentage that their allowed claims represent with regard to the total amount of the allowed claims. The reorganisation plan must satisfy certain requirements, such as containing a payment schedule that comprehends all of the insolvency claims (whether allowed or not) and a provision that states that at least 30 per cent of all funds used to pay pre-publication claims on an annual basis, will be used to pay labour claims.

During the reorganisation process, the creditors' meeting may decide to keep the debtor 'in possession' or replace, partially or totally, the debtor's management. The creditors' meeting replaces the shareholders' meeting in its duties and rights. The reorganisation process does not end until the Commission verifies that all claims (allowed or not) have been paid, which, in practice, means that the debtor will remain under the regulations of the Insolvency Law for the maximum term established in the reorganisation plan for the payment of pre-publication claims.

##### Preventive proceeding

The preventive proceeding is conceived as a fast-track proceeding that can only be initiated by the debtor (for requirements to initiate the proceeding see question 1). The sole purpose of the preventive proceeding is to set an appropriate forum for the debtor to reach a debt financing

arrangement with its creditors. Automatic stay is available, depending on the debtor's request.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

See questions 9, 10 and 11.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

The Insolvency Law does not contain regulations that establish the mandatory commencement of insolvency proceedings.

However, the General Corporations Law provides that the board of directors is obliged to inform the shareholders immediately when it becomes aware or suspects the existence of losses in excess of 50 per cent of its share capital. Moreover, if the assets of the company are insufficient to cover its liabilities or if such insufficiency is suspected, the board should immediately summon the shareholders to a general shareholders' meeting to inform them of the situation and, within 15 calendar days of such a summons, notify the company's creditors and commence an insolvency proceeding according to the Insolvency Law provisions. If the board of directors does not comply with its obligation, the directors may be liable before the company, the shareholders and third parties for any proven damages and losses caused as a consequence of such a breach. Any such liability would have to be reviewed by the judiciary on a case-by-case basis.

Moreover, pursuant to the General Corporations Law, if the company suffers losses that reduce its net patrimony to less than one-third of its paid-in share capital, the company must be dissolved and liquidated (under the rules set out in the General Corporations Law). In cases where the company continues in business despite incurring in this dissolution cause, officers and representatives of the company may be held personally and jointly liable (with the company) for the agreements and acts entered into since incurring in the dissolution cause.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

Under a reorganisation proceeding, debtors will always be allowed to carry on their business and activities. However, the reorganisation plan or the creditors' meeting may impose certain limitations that must be complied with.

If fixed assets are sold during a reorganisation, the priority (rank) applicable in a liquidation proceeding will apply (see question 33).

The Insolvency Law does not establish any special treatment to creditors who supply goods or services during the reorganisation. Special treatment for those creditors is usually established in the reorganisation plan but for their credits originated before the bar date (eg, for their pre-publication claims, not for the new credits that might be provided to the debtor during the reorganisation).

In general, the role of creditors (through the creditors' meeting) is central in reorganisations. The creditors' meeting replaces the shareholders' meeting, has the right to designate and replace the debtor's administration, modify its by-laws, designate directors, approve mergers and any other agreement necessary for the administration of the debtor.

INDECOPI is not involved in the supervision of the debtor's business activities. However, the debtor's administration is obliged to file quarterly reports to INDECOPI informing about the principal aspects related to the business and the compliance of the reorganisation plan. INDECOPI can impose fines if such reports are not filed.

Before the creditors' meeting is convened, directors and officers can exercise the ordinary powers and faculties inherent to their positions. However, the Insolvency Law has identified certain actions that may be declared void if taken during the avoidance period (see question 39). Once the creditors' meeting is convened and adopts a decision regarding the debtor's administration (eg, to ratify or appoint new directors and officers), directors and officers can exercise the powers or faculties conferred to them by the creditors' meeting or by law (subject to the limitations that the creditors' meeting or the reorganisation plan might impose).

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

From the bar date, all obligations of the debtor become temporarily unenforceable. The automatic stay suspends enforcement of any pre-publication claim against the debtor's estate until a reorganisation plan or liquidation plan is approved. In addition, from the bar date, all execution proceedings for collection as well as injunctions (related to pre-publication claims) against the debtor's estate are stayed. Certain special rules apply regarding guaranties over perishable goods and warrants (see question 44).

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

In the case of reorganisation proceedings, a debtor may obtain loans and grant guarantees provided that such agreements are approved, directly or indirectly, by the creditors' meeting (or through the reorganisation plan). Any credit obtained after the bar date will be considered as post-publication claims and will not be included in the reorganisation proceeding. Those new credits will be part of the insolvency proceeding only if the debtor ends up being liquidated and will not have any particular priority or privilege in the liquidation proceeding.

Provided that a liquidation as a going concern has been approved by the creditors' meeting, loans or credits originated during that period (and related to the continuity of activities of the debtor) will be considered as expenses of the liquidation and will have priority over all other claims.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

The Insolvency Law has established a ban on compensations or set-offs by declaring that compensations entered into by a debtor during the avoidance period (as defined in question 39) may be declared void by the judiciary (it does not require a cause). Moreover, given that from the bar date, the debtor's obligations will be unenforceable, it will not be possible to offset credits against the debtor.

In the case of reorganisations, the reorganisation plan could establish mechanisms that allow extinguishing obligations through set-offs.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

In the case of reorganisations, the sale of fixed assets requires approval of the creditors' meeting or an authorisation through the reorganisation plan, in the event that the debtor's management does not already have express faculties to sell fixed assets. There are no provisions for

the purchaser to acquire the assets 'free and clear' of claims. There are no restrictions for 'stalking horse' bids or 'credit bidding', however, such types of agreements must be approved by the creditors' meeting or authorised by the reorganisation plan. Finally, there are no express legal restrictions for selling the entire business in a reorganisation (provided that the creditors' meeting has approved the agreement), nonetheless, in our opinion, depending on the particular characteristics of the agreement, post-publication creditors and shareholders could challenge such kinds of agreements before the judiciary. A case-by-case analysis would be required.

In the case of liquidation proceedings, it is possible to sell specific assets or the entire business as a going concern. In both cases, the purchaser will acquire the assets 'free and clear' of liens as it is expressly stated in the Insolvency Law. Provided that the liquidation plan specifically allows the figures and a public auctioneer participates in the bids, it would be possible to establish 'stalking horse bids'; however, if the debtor's assets are subject to precautionary measures, charges or liens, such assets can only be sold in public bids. Special provisions must be included in order to protect labour creditors (according to the Peruvian Constitution labour rights may not be waived).

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

The Insolvency Law does not contain special provisions associated with IP rights. Parties' rights and relations will be governed by the corresponding contract.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Insolvency Law does not contain any special provisions in relation to the use or transfer of personal information or customer data within an insolvency proceeding. However, the Personal Data Protection Law, Law No. 29733, regulating the treatment of personal and sensitive data, does contain general provisions regarding the use and transfer of said information.

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### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

The Insolvency Law does not entitle the debtor to terminate or reject contracts, unfavourable or not, to which it is a party. Such types of decisions are analysed, taking into consideration the provisions established in each contract on a case by case basis. Similarly, any breach of contract occurring after the bar date, shall be governed by the provisions of the contract.

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### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Under Peruvian law, insolvency proceedings cannot be carried through arbitration proceedings. INDECOPI is the only competent authority to administer insolvency proceedings involving debtors domiciled in

Peru. Arbitration is expressly allowed only in relation to disputes associated with the execution and interpretation of a reorganisation or liquidation plan.

If a party to an ongoing arbitration is subject to an insolvency proceeding, the arbitration will continue in order to determine (through an award) the existence and amount of any pre-publication obligation of the insolvent party. The creditor shall register the controversy with the Commission through a proof of claims proceeding (see question 31). Because of the insolvency proceeding effects, the award will not be enforceable against the debtor. The creditor who obtains a favourable award establishing a credit against the insolvent debtor shall file the award with the Commission in order to vary its credit status from 'contingent' to 'allowed'.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

For the approval requirements, see question 11.

The principal requirements of the reorganisation plan are that it shall include:

- a payment schedule that comprehends all the pre-publication claims, including not allowed pre-publication claims (because the respective creditor did not file a proof of claims petition before the Commission);
- provisions that establish that at least 30 per cent of all funds used to pay pre-publication claims on an annual basis will be used to pay labour claims;
- projected cash flows; and
- accounting provisions for the payment of contingent claims.

Within reorganisation proceedings, there are no specific rules for the classification of creditors. The creditors' meeting can establish different classifications based on reasonable economic criteria, the priority and specific characteristics of the creditors and their roles on the success of the reorganisation plan. Special regulations apply for the classification and payment of labour credits (which cannot be subject to haircuts) and also to tax credits (tax credits shall have the same treatment applicable to the class in which the higher percentage of creditors is incorporated, cannot be capitalised or be subject to haircuts).

The Insolvency Law does not contain any provision that allows the creditors' meeting to release non-debtor parties from liabilities. In any case, the validity and legality of any such release would have to be determined on a case-by-case basis.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

No. The most expeditious insolvency proceeding is the preventive proceeding (see question 11).

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

INDECOPI may declare the nullity of any reorganisation plan that does not satisfy the legal requirements (see question 23), either on its own initiative or at the challenge of allowed creditors representing at least 10 per cent of the allowed claims. Allowed creditors can challenge the reorganisation plan within 10 business days from the date of its approval by the creditors' meeting. INDECOPI can declare the nullity of the reorganisation plan within 30 business days from the date of its approval by the creditors' meeting.

If the debtor fails to perform the plan, INDECOPI can declare the liquidation of the debtor. Such declaration of liquidation can be made at the request of an allowed creditor or by INDECOPI (when the breach of the reorganisation plan was declared by the debtor).

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The first notice that creditors receive is the publication in the official gazette informing that the debtor has been declared insolvent. Various other notices could be given to creditors throughout the proceeding, including, but not limited to, the approval or refusal of their proofs of claim, the date and time of any creditors' meeting, and any disputes against their proofs of claim, among others.

There is no limitation on the number of times that a creditors' meeting can be held. The meetings held during an ordinary proceeding include the meeting to approve the debtor's reorganisation or liquidation, the meeting to approve the debtor's reorganisation or liquidation plan; and the meeting to ratify or replace the debtor's administration or liquidator. The creditors' meeting shall appoint a creditor to act as president, who will be in charge of calling the meetings; creditors representing 10 per cent of allowed claims can also request a creditors' meeting to the president of the creditors meeting, and if the president does not comply with such request, to INDECOPI.

All allowed creditors have access to the files of the proceeding (including other creditors' files and those containing information filed by the debtor). The debtor's administration or liquidator is obliged to file quarterly reports to INDECOPI on the principal aspects of the business and the compliance of the reorganisation or liquidation plan.

In general, the debtor's administration or its liquidator has the right to pursue the estate's remedies against third parties. However, consider that: the Insolvency Law expressly authorises creditors to pursue the estate's remedies in connection with claims regarding the avoidance and suspect periods (see question 39); and, pursuant to article 1219.4 of the Peruvian Civil Code, creditors are entitled to enforce its debtor's rights (or assume its defence) without requiring previous judicial authorisation. Although the Insolvency Law does not contain references to this specific action, we do not see limitations for being it utilised by creditors in the context of an insolvency proceeding. The fruits of any of these remedies will belong to the debtor.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

See question 26.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

In ordinary proceedings, the creditors' meeting may designate a creditors' committee from within its members and delegate all its powers, with the exception of the power to decide on the reorganisation or liquidation of the debtor and the power to approve the reorganisation or liquidation plan (and their amendments). The creditors' committee shall be formed of four members (creditors) each representing, if possible, different types of credit. The president of the creditors' meeting shall also preside over the creditors' committee.

The committee members will be liable before creditors, shareholders and third parties for any damage caused through the approval or execution of agreements or contracts that violate the law or the debtor's by-laws, or are incurred with deliberation, gross negligence or abuse of their faculties.

There are no limitations for the committee members to retain advisers, however, their expenses shall be funded by the creditors that are members of the committee (not by the debtor).

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## Insolvency of corporate groups

- 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

The Insolvency Law does not recognise corporate group insolvency. Hence, in order for a Peruvian company to be declared insolvent, it is required that the company, individually, satisfies the insolvency criteria under the Insolvency Law to be declared insolvent (either through a voluntary or involuntary request), none of which relates to insolvency of a shareholder, a subsidiary or any related party to the insolvent company. Regarding the transfer of assets from Peru to a foreign jurisdiction, see question 47.

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## Appeals

- 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

Peru has an administrative insolvency system (see question 2). In that sense, the right to file reconsideration or appeal recourses within an insolvency proceeding applies to administrative resolutions issued by the Commission in the first instance.

Within an insolvency proceeding, the debtor, creditors holding allowed claims or third parties appearing at the proceeding have the right to file a reconsideration recourse before the Commission or an appeal before the INDECOPI's Tribunal in order to challenge administrative resolutions issued by the Commission that resolve definitely on the merits. The reconsideration or appeal recourse will be admitted by the competent instance if the interested party is able to identify an error within the administrative resolution and the damage it causes. The reconsideration recourse is supported on the existence of new evidence, while the appeal recourse is supported on a different interpretation of the existing evidence or the applicable laws. The reconsideration or appeal recourse must be filed within five business days of being notified of the relevant resolution.

No prior permissions are required for contesting an administrative resolution.

Contentious administrative judicial review proceedings can be commenced in order to challenge INDECOPI's Tribunal decisions (special procedural rules will apply).

The Insolvency Law does not establish any requirements to post security to file an appeal or reconsideration recourse.

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## Claims

- 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

In order to be allowed to participate in the ordinary or preventive proceedings, pre-publication creditors shall file before INDECOPI their proofs of claim, in writing within 30 business days from the bar date. With exception of labour credits, creditors must pay an administrative fee to INDECOPI in order for such entity to process, evaluate and – as the case may be – allow their claim.

Claims filed after the referred period will be allowed by INDECOPI but will not be entitled to vote in the creditors' meeting unless the debtor ends up being liquidated. It should be noted that if a creditor does not file a proof of claim, the payment of its credit, either in a reorganisation or liquidation or in a preventive proceeding, will be subordinated to the payment of all allowed claims (independently of its priority). Special provisions apply in the case of labour claims.

If INDECOPI disallows the creditor claim, the creditor has the right to file a reconsideration recourse before the Commission or an appeal before INDECOPI's Tribunal. Contentious administrative judicial review proceedings can be commenced in order to challenge INDECOPI's Tribunal decisions (special procedural rules will apply).

Contingent creditors who file their proof of claim will be registered by INDECOPI as such. Although contingent creditors who filed their proofs of claim within 30 business days after the bar date can attend (and participate in) the creditors' meetings, their voting rights will be suspended until their claims stop being contingent (that is, until the pending judicial, administrative or arbitral proceeding comes to an end with a favourable result for the creditor) and are allowed by INDECOPI.

The transfer of claims is expressly allowed by the Insolvency Law (no restrictions apply). The creditor that transfers its claim shall inform INDECOPI of the transfer.

Claims acquired at a discount can be enforced for their full face value. It is also important to note that, pursuant to the Insolvency Law, the transfer of a claim entails the transfer of its corresponding order of priority.

In reorganisation proceedings, creditors holding pre-publication claims can only claim interests accrued until the bar date. Interests of pre-publication claims accrued from the bar date forward will be governed by the provisions of the reorganisation plan. In liquidation proceedings, creditors may claim interests accrued before and after the bar date. However, interests accrued after the bar date will be governed by the provisions of the liquidation plan.

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## Modifying creditors' rights

- 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

INDECOPI does not have the faculty to change the rank of a creditor's claim. However, creditors (different from labour and tax creditors) can waive their priority.

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## Priority claims

- 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Within a liquidation proceeding, the liquidator must mandatorily pay the allowed claims in the following priority order:

- first: labour claims (included pension claims);
- second: alimony claims (applicable only when the insolvent is an individual);
- third: secured claims (ie, creditors secured by mortgages, pledges, attachments, seizures or precautionary measures);
- fourth: tax claims; and
- fifth: non-secured claims.

This order of precedence is not of mandatory application in reorganisations and preventive proceedings.

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## Employment-related liabilities in restructurings

- 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

The Insolvency Law does not provide any particular regulation that allows the termination of employment contracts in a reorganisation context (nor in preventive proceedings).

In a liquidation context, the Insolvency Law contains provisions that allow the debtor to terminate labour contracts in a collective manner. Labour credits that arise after such termination will have priority (first priority) in the liquidation proceeding.

The priorities granted to labour credits are expressly recognised in the Peruvian Constitution, which establishes a super-priority for such type of credits.

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**Pension claims**


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**35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Pension-related credits have the same priority as labour credits (first priority). However, commissions owed by the debtor to private pension funds have a fifth order of priority.

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**Environmental problems and liabilities**


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**36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

The Insolvency Law does not contain any provision regarding environmental problems and liabilities. Such obligations and liabilities will continue to be governed by the applicable environmental regulations. To the extent that they qualify as pre-publication claims, credits derived from environmental liabilities should be allowed as unsecured claims within the proceeding (unless that prior to the bar date, the environmental authority obtained a security or collateral – such as an attachment or seizure – to secure the payment of such claim, in which case it should be allowed as a secured claim).

Remediation liabilities and responsibilities shall be analysed on a case-by-case basis.

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**Liabilities that survive insolvency proceedings**


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**37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

In reorganisation, post-publication credits will 'survive' the proceeding as those credits are not part of it (see question 9). As mentioned in question 46, a reorganisation concludes with the payment of all pre-publication claims.

After the conclusion of the liquidation, creditors may enforce their credits against the liquidator only if the liquidator is responsible for the lack of payment. Such a responsibility shall be established in a judicial proceeding. Without prejudice to statute of limitation regulations, credits will not be technically extinguished after the conclusion of the liquidation proceeding and the extinction of the debtor.

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**Distributions**


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**38 How and when are distributions made to creditors in liquidations and reorganisations?**
**Liquidations**

The exact terms of how and when the distributions shall be made will be established in the liquidation plan. The liquidation plan shall respect the general framework for distributions in liquidation proceedings established in the Insolvency Law. Besides the priority order mentioned in question 33, the following principal rules apply:

- the liquidator shall start making payments to the creditors when at least an amount representing 10 per cent of the total allowed claims has been obtained through the sale of the debtor's assets;
- the liquidator shall first pay the allowed credits, respecting the priorities established in the Insolvency Law;
- labour credits shall be paid *pari passu* taking into consideration the percentage that each labour credit represents in relation to the total amount of credits incorporated in the class; and
- all other credits (different from secured credits) shall be paid *pari passu* in relation to the credits incorporated in each class.

Secured credits shall be paid with the proceeds of the foreclosure of their respective collateral, unless such collateral has been sold and the proceeds have been used to pay labour or alimony claims (which are senior in relation to the secured creditor). In those cases, all the creditors that hold collateral participate *pari passu* in relation to their contribution for the payment of the credits ranked above them. If there should be any unpaid remnant, such amount is paid *pro rata* with non-secured claims.

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**Reorganisations**


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Distributions to creditors within a reorganisation process shall be made in accordance to the payment schedule and dispositions or terms set for each class of creditor (such as interest payments) contained in the reorganisation plan approved by the creditors' meeting. Also, such payment schedule must contain a provision that states that at least 30 per cent of all funds used to pay pre-publication claims on an annual basis will be used to pay labour claims. Labour claims shall be paid equally within the number of creditors holding labour claims. On the other hand, creditors holding tax claims shall be paid in accordance to the conditions set for the class with the most allowed claims. In addition, the reorganisation plan may contain provisions for the condonation, novation or capitalisation of allowed claims.

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**Transactions that may be annulled**


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**39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Under the Insolvency Law, once the debtor files for its insolvency, or is given notice of an involuntary filing, all actions by management during the previous year (suspect period) and from that date on and until the date the creditors ratify or replace management (avoidance period) are put under scrutiny with two different tests. These tests may result in such actions being declared void.

The first test covers all actions or transactions, whether for consideration or not, performed during the suspect period. These will be declared void if they have a negative effect on the net worth of the company and are not related to the regular activities of the debtor (both requirements must be met).

The second test covers the following actions by management if they happen during the avoidance period:

- payment of unmatured obligations;
- payment of mature obligations not made according to their terms;
- contracts for consideration that are not in the ordinary course of business;
- compensations (set-offs) among mutual obligations with creditors (see question 17);
- liens over, or transfers of, property;
- liens created in security of obligations incurred before insolvency;
- foreclosure on liens and attachments; and
- mergers and spin-offs if they have a negative effect on the net worth of the insolvent.

After declaring an act or contract void, the court will order the return of the property to the insolvent party or the termination of the lien, as the case may be.

An action against a particular act or contract may be brought before a court by the designated administrator, replacing management or by any creditor holding an allowed claim.

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**Proceedings to annul transactions**


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**40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

See question 39.

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**Directors and officers**


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**41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

Pursuant to the General Corporations Law, corporate officers and directors are liable before the corporation, shareholders and third parties for any damages arising from the non-compliance of their obligations or the performance of acts (resulting from the agreements adopted with their votes in the case of directors) against the law, the by-laws, acts of fraud, gross negligence or those resulting from the abuse of their faculties.

Particularly, the general manager (CEO) is subject to criminal responsibility, in addition to the civil liability.

Managers may be jointly and severally liable with the companies before the tax authorities when tax debts are not paid because of manager's gross negligence, fraudulent acts with the intent to cause harm or abuse of powers. Gross negligence, fraudulent acts with the intent to cause harm and abuse of powers are presumed by the law for several actions and cases expressly specified in article 16 of the Tax Code, such as the lack of an accounting system in a company, or such a company not being registered before the tax authorities, among others.

The Insolvency Law does not establish sanctions for officers and directors (eg, disqualification).

The Criminal Law Code establishes criminal responsibility for management (liquidators and creditors can also be responsible in certain circumstances) if they engage in certain conduct associated to insolvency scenarios (eg, concealment of property, simulation of debts, among others).

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

There are no regulations establishing that parent or affiliated companies are responsible for subsidiaries' or affiliates' liabilities (see question 29).

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There are no restrictions for insider creditors obtaining the allowance of their credits by INDECOPI. However, when deciding to allow a proof of claim filed by an insider creditor, INDECOPI must verify the existence, legitimacy and amount of the alleged claims by all means it deems appropriate (the highest standard of proof applies). See question 11 in relation to special provisions applicable if the total amount of insider credits exceed 50 per cent of the total amount of allowed credits.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

The general rule is that from the bar date, all proceedings (associated with pre-publication claims) related to seizures or attachments of the debtor's assets are suspended. However, special regulations apply in the case of perishable goods (the goods can be sold but the proceeds shall be put at the disposal of the new administration or liquidator). Special regulations also apply in the cases of warrants granted to entities that are regulated by the General Law of the Financial and Insurance Systems.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

The General Corporations Law establishes a corporate procedure in order to liquidate a company.

The main differences between such procedure and the liquidation proceeding regulated in the Insolvency Law are that the decision to liquidate the company is always in hands of the shareholders, who remain in control of the company throughout the procedure (there is no creditors' meeting), any individual or company can be appointed as liquidator, there is no automatic stay, there is no proof of claims proceeding, there are no suspect or avoidance periods and there is no participation of INDECOPI. Creditors are able to initiate an ordinary insolvency proceeding (under the Insolvency Law) in respect of companies that are already under a liquidation proceeding under the General Corporations Law (in which case such liquidation proceeding will be stayed during the duration of the insolvency proceeding).

### Update and trends

In August 2015 the Insolvency Law was amended by means of Legislative Decree No. 1189. The amendments introduced by Legislative Decree No. 1189 came into force on 20 October 2015, with the exception of a disposition regarding the term of liquidations as a going concern, which came into force on 22 August 2015 (ie, on the date following that of the publication of the Legislative Decree in the official gazette). In addition, in August 2016, Law No. 30502 was enacted in order to authorise extraordinary extensions to the term set in the Insolvency Law for liquidations as a going concern. To the best of our knowledge, there is no pending legislation affecting domestic bankruptcy procedures, international bankruptcy cooperation or recognition of foreign judgments and orders.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

##### Reorganisations

When all pre-publication claims (allowed or not) are paid according to the reorganisation plan terms, INDECOPI grants a decision declaring the formal conclusion of the reorganisation proceeding.

##### Liquidations

If all creditors are paid, the liquidator files a petition before the Public Registry in order to register the extinction of the company. If creditors remain unpaid after the liquidation of all the debtor's assets, the liquidator will file a petition before a civil judge in order to obtain a judicial bankruptcy declaration. Such a declaration is published in the official gazette for two consecutive days. After the publication, the 'extinction of the debtor's patrimony' is registered in the Public Registry.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

The UNCITRAL Model Law on Cross-Border Insolvency has not been adopted and, to the best of our knowledge, it is not under consideration at this moment in Peru. Current legislation regarding international insolvency scenarios is principally contained in the 1984 Civil Code and the Insolvency Law.

Recognition and relief for foreign insolvency proceedings is available provided that the debtor is not domiciled in Peru. An exequatur proceeding is commenced (before the judiciary) if there are assets of the foreign debtor located in Peruvian territory. The competence of the Peruvian authorities is exclusively related to the assets located in Peruvian territory.

After the judicial recognition is granted, an ancillary insolvency proceeding will be commenced before INDECOPI according to the rules settled in the Insolvency Law (publication in the official gazette, proofs of claims, creditors' meetings, etc). Although the Insolvency Law does not establish any kind of differentiation between national and foreign creditors, the 1984 Civil Code still establishes a preference for domiciled creditors and credits registered in Peru. In our opinion, such provision is incompatible with the 1993 Peruvian Constitution, which expressly states the equality between national and foreign investment and, therefore, legal actions could eventually be taken in order to avoid its application, if necessary.

If no creditors requested payment in Peru or if after paying those creditors who requested payment there were proceeds obtained from the foreclosure of the assets, such proceeds should be sent to the foreign administrator only if, previously, the foreign administrator obtained a judicial recognition (by a Peruvian judge) of the existence of credits in the foreign jurisdiction.

In cases in which a treaty exists, such a treaty shall be applied. Peru is signatory of the following treaties related to recognition of foreign judgments and international insolvency: the Montevideo Treaty (1889), the 1928 Havana Convention (Bustamante Code), and the Inter-American Convention on Extraterritorial Validity of Foreign Judgments and Arbitral Awards (1979).

#### COMI

**48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

The Insolvency Law does not provide any kind of test to determine the COMI. For purposes of determining the competence of INDECOPI's offices in Peruvian territory, the Insolvency Law establishes that companies are domiciled where it is stated in their respective by-laws duly registered in the Commercial Public Registries. As previously mentioned, the Insolvency Law does not recognise insolvency proceedings of a corporate group.

#### Cross-border cooperation

**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

There are no legal provisions that allow cross-border cooperation. See question 47.

#### Cross-border insolvency protocols and joint court hearings

**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

There are no legal provisions that allow cross-border insolvency protocols and joint court hearings.

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# Romania

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The main piece of legislation applicable to legal entities is Law No. 85/2014 regarding insolvency prevention mechanics and insolvency proceedings (the Insolvency Law).

Insolvency is characterised by the insufficiency of available funds for the payment of certain, determined and due receivables. The debtor's insolvency is presumed if the debtor has not paid its debts, above certain thresholds set by the Insolvency Law, to its creditors for more than 60 days from the debts' due date.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The competent court to decide on the opening of insolvency proceedings is the tribunal having jurisdiction over the location where the debtor had its registered office at least six months prior to the filing. The court competent to assess appeals is the Court of Appeal.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

Although the Insolvency Law is of general applicability, it does not apply to educational entities and institutions, as well as assimilated entities as per the relevant applicable legislation, for which no relevant provisions seem to be established. The Insolvency Law does not apply to professionals conducting liberal professions (such as doctors, architects, lawyers, etc).

The Insolvency Law does not exclude any specific assets from its scope.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

No special procedures are followed in the insolvency of government-owned enterprises. The common procedure is followed in this case and therefore no specific remedies are established for creditors in this particular situation. We describe the general remedies below (see question 8).

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No. The legislation currently does not provide for special treatment with respect to particular institutions and takes rather a holistic approach towards the general applicability of the Insolvency Law's provisions to all categories of debtors (as mentioned above). Also, the

concept of institutions considered 'too big to fail' is not regulated under Romanian law.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immoveable (real) property?

Immoveable (real) property may be charged by means of immoveable hypothec agreements.

Security over immoveable assets must be registered with the relevant land book registry held at the location of the respective immoveable assets.

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## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

There are multiple types of security available for charging moveable (personal) property, such as: hypothec over moveable assets (including receivables, insurance policies, intellectual property, equipment, vehicles, raw materials and stocks etc); hypothec over the bank accounts opened with Romanian credit institutions; and hypothec over the shares and related rights.

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## Unsecured credit

### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Unsecured creditors (either domestic or foreign) may make use of attachments and seizures over the assets of their debtors. Their use is generally accessible and not time-consuming, as the Civil Procedure Code provides short procedural terms to speed up the process.

If an asset subject to an attachment had been previously charged with security, the secured creditors are notified in relation to the attachment and will be invited to all proceedings involving the respective assets. Also, the attachment will be registered with the Electronic Archive for Moveable Security and the other relevant registries. From the moment the assets are blocked through the attachment, the debtor is unable to dispose of them during enforcement proceedings.

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## Voluntary liquidations

### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

There is no automatic placing into liquidation of insolvent debtors, as liquidation is a phase that is decided by the insolvency judge in certain cases, such as when the debtor has declared his intention of opening the simplified procedure, or when it has not declared intention to enter into reorganisation and no other entities entitled to propose a reorganisation plan has done so (or, even if this happened, the proposed plan was not accepted and confirmed), etc.

The effects of liquidation imply the prohibition of the debtor to manage its business, the sale of the debtor's assets and the distribution of the proceeds resulting from the sale to its debtors, according to the imperative order established by the law.

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**Involuntary liquidations**
**10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

See question 9.

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**Voluntary reorganisations**
**11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

We will refer to how insolvency proceedings are commenced, as reorganisation is just one possible phase of insolvency.

A debtor is obliged to file for insolvency if it is in an insolvent state (as characterised above).

The debtor may propose a reorganisation plan only based on the approval of the general meeting of shareholders and within 30 days from the date when the final receivables list was published, but only if it declared this intention when filing for insolvency.

The opening of the insolvency procedure has a series of effects, such as:

- the automatic stay of all judicial and extrajudicial proceedings against the debtor;
- penalties and interests cease to accrue against the debtor;
- the providers of 'vital services' are no longer entitled to terminate their contracts with the debtor;
- the liquidator or judicial receiver is entitled to 'cherry pick' the ongoing agreements it wants to continue and may amend ongoing agreements; and
- all transactions and payments are null and void unless allowed by the law or approved by the insolvency judge; legal set-off and derivatives netting are, however, allowed, etc.

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**Involuntary reorganisations**
**12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

A minimum threshold related to indebtedness must be observed when creditors file for insolvency. Thus, any request for opening insolvency proceedings must refer to a receivable having a minimum value of 40,000 leu (the minimum threshold).

Creditors are allowed to file for insolvency with respect to receivables they hold against their debtors, subject to the following conditions:

- the minimum threshold is observed;
- the creditors' receivables are certain and determined, and have been due for more than 60 days; and
- the debtor's insolvency is presumed (ie, the debtor has not paid its debts to creditors for more than 60 days from the due date).

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**Mandatory commencement of insolvency proceedings**
**13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

Yes, as mentioned above, a debtor is obliged to file for insolvency if it is in an insolvent state.

If the filing is not made or it is made within a term that exceeds the legal term by more than six months, the legal representatives (directors) of the debtor are subject to a criminal offence punishable with either imprisonment (from three months to one year) or with a criminal fine.

A company is free to carry on its business while insolvent (with no insolvency procedure being opened). The consequence of not declaring its insolvency is related to the criminal liability of its legal representatives.

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**Doing business in reorganisations**
**14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

The debtor can carry on business during reorganisation by or under the supervision of the judicial receiver and the insolvency judge and in accordance with the confirmed reorganisation plan. Any act (including sale of assets) that does not fall under the usual, day-to-day activities of the debtor must be authorised by the judicial receiver after approval by the creditors' committee.

Generally, acts concluded during the reorganisation period confer a special status to creditors. For example, any financing arrangements granted to the debtor for the purpose of conducting its usual business, if approved by the creditors, benefit from priority at repayment. Also, creditors holding against the debtor any certain, determined and due receivables that arise after the opening of the insolvency proceedings and that exceed the minimum threshold are entitled to request the liquidation of the debtor.

If the debtor has not declared its intention to reorganise, the opening of the insolvency procedure triggers the loss of the right to administer the company (which includes the right to conduct its activity and to manage and dispose of its assets). Also, creditors or the judicial receiver may request the insolvency judge to deprive the debtor of its administration right if they can prove ongoing losses affecting the debtor's estate or the improbability of realising a rational business plan.

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**Stays of proceedings and moratoria**
**15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

Once the insolvency proceedings are opened, all judicial and extrajudicial actions and enforcement procedures are automatically suspended and the realisation of third parties' rights is achieved as part of the insolvency proceedings.

Nonetheless, secured creditors have the right to lift the suspension of claims with regard to their debts. This, however, can only be done if either certain conditions are cumulatively met (ie, the value of the secured asset is fully covered by the total value of the secured receivables, the secured asset is not vital for the success of an envisaged reorganisation and the secured asset can be safely disposed of separately) or if the secured claim is not properly protected (because of, for example, a reduction in the value of the secured property or the existence of a real danger that the value of the secured property would diminish considerably).

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**Post-filing credit**
**16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

Yes, this is possible. All financing facilities granted to the debtor for the purpose of conducting its usual business, if approved by the creditors, benefit from priority at repayment. This means that such receivables come immediately after the taxes and other expenses related to the sale of the debtor's assets or advanced by creditors as part of the insolvency proceedings.

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**Set-off and netting**
**17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

The opening of insolvency proceedings does not impact the right of creditors to invoke the legal set-off of their receivables and their debtors' receivables (as opposed to contractual set-off, which may be

prevented if the judicial receiver so decides). At the same time, the Insolvency Law recognises the netting in case of ISDA master agreements and similar master set-off arrangements. Creditors cannot be deprived of this right.

### Sale of assets

- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

As previously mentioned, any act or operation (including the sale of assets) that does not fall under the ordinary course of business of the debtor must be authorised by the judicial receiver after approval by the creditors' committee. If the transferred assets are encumbered, the purchaser acquires them as such.

The sale procedure is generally strictly regulated by Romanian legislation and does not allow for deviations. For example, immoveable assets are sold based on public auction and aspects such as 'stalking horse' bids are not compatible with the sale procedure.

Creditors may adjudicate the moveable or immoveable assets owned by the debtor in exchange for all or part of the receivables. By adjudicating the debtor's moveable or immoveable assets, the creditor becomes the owner of such assets and the value of the receivables is reduced with the price of the adjudicated assets.

Creditors may adjudicate a moveable asset owned by the debtor in exchange of all or part of the receivables at the price established by the bailiff in the notice of sale published for the final auction term. However, if the asset is not sold during the first auction term, the starting price of the auction decreases by 25 per cent for every subsequent term, but cannot be lower than 50 per cent of the starting price of the first auction term.

Creditors may adjudicate an immoveable asset owned by the debtor in exchange for all or part of the receivable at a value less than 75 per cent of the starting price of the first auction (ie, price determined according to the valuation performed by the expert assessor).

### Intellectual property assets in insolvencies

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

According to Romanian law, any contractual clauses concerning the termination of an agreement because of the commencing of insolvency proceedings against a party are null and void. Nevertheless, an IP licensor or owner may terminate an agreement with the debtor (against whom insolvency proceedings have commenced) if the clauses therein provide the possibility to unilaterally terminate such agreement (eg, subject to a notice period).

A judicial receiver may decide that the debtor should continue to use the IP rights granted under an agreement between the debtor and the IP licensor or owner during the contractual term agreed by the parties. Alternatively, the judicial receiver may decide to unilaterally terminate the respective agreement if it considers the agreement not beneficial for the debtor and if the agreement has been only partially performed or not yet performed.

Following the termination of an agreement concluded between an IP licensor or owner and the debtor undergoing insolvency proceedings, the debtor may not continue to use the IP rights for the benefit of its estate (except if provided otherwise in the agreement), as generally the obligation of the IP licensor or owner under an agreement to grant the debtor right of use over its IP rights ceases when the agreement is terminated.

### Personal data in insolvencies

- 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Customer personal data can be transferred to a third party or otherwise used in a commercial manner (required for its successful reorganisation) depending on whether the customer's consent has been obtained. Transfer of customer personal data to third parties outside the European Union requires an additional approval from the data protection regulator.

### Rejection and disclaimer of contracts in reorganisations

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

As a rule, any contractual clauses providing for the termination of ongoing contracts or acceleration for the reason of the commencing of the insolvency procedure are invalid. However, the judicial receiver or liquidator may terminate, within three months from the opening of the insolvency procedure, any ongoing contract for as long as it has not been substantially performed by all its parties.

Also, the judicial receiver or liquidator must respond within 30 days from receipt of the termination request served by the debtor's contractors within the above three-month period. If there is no response, the contract is deemed terminated and the judicial receiver or liquidator can no longer require its performance. Contractors may claim indemnification from the debtor for the termination of the contracts and the insolvency judge will rule over the respective claim. At the same time, contractors may claim the unilateral termination of the contracts maintained by the judicial receiver for contractual breaches attributable to the debtor.

The debtor loses the benefit of term for performing its contractual obligations if, within three months from the opening of the insolvency proceedings, its contractor notifies the judicial receiver or liquidator of its intention to terminate the respective contract or accelerate the due payments.

The Insolvency Law also contains specific provisions for certain types of contracts (such as labour agreements, rent agreements) based on which the termination mechanics are further detailed and circumstantiated.

Agreements concluded with service providers for the supply of electricity, natural gas, water and other types of facilities cannot be changed or suspended during the period of observation or reorganisation, provided the debtor is a captive consumer pursuant to the law (ie, a consumer which benefits from a regulated agreement with its supplier).

### Arbitration processes in insolvency cases

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Under Romanian legislation, insolvency proceedings fall under the jurisdiction of the competent national tribunal. According to the Insolvency Law, following the opening of the insolvency proceedings, all pending judicial and extrajudicial proceedings filed against the debtor's assets, as well as all enforced execution measures for the recovery of debts, are automatically suspended. This provision is also applicable in case of arbitration proceedings.

The arbitral tribunals must apply the provisions of the Insolvency Law, which are mandatory and protect the public order of the forum, specifically in order to avoid the arbitral decision being annulled. Thus, the arbitration clause as a principle cannot prevail over the necessity of equality for all unsecured creditors.

According to the Insolvency Law, the following claims filed by creditors against a debtor undergoing the insolvency procedure are not automatically suspended (applicable also in arbitration proceedings):

- claims for recognition of rights of the creditor;
- claims concerning property rights; and
- claims concerning the annulment of an agreement concluded between the debtor and the creditor.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

A reorganisation plan must contain the receivables payment schedule and the adequate measures for its implementation. Also, the Insolvency Law requires that certain information be specified in a reorganisation plan, such as the treatment of disadvantaged receivables, means for payment of current receivables, etc.

There are five categories of receivables by reference to which their creditors vote separately:

- receivables benefiting from preference rights;
- wage receivables;
- budgetary receivables;
- receivables of indispensable creditors; and
- other unsecured receivables.

The reorganisation plan shall be deemed to be accepted by a category of receivables if in the relevant category the plan is accepted by the absolute majority in that category. In computing the absolute majority, only the value of the receivables, and not the number of creditors, will be taken into consideration.

The reorganisation plan shall be confirmed by the insolvency judge provided that all of the following conditions are met:

- at least three, two or half (depending on the number of categories) of the categories of receivables listed in the payment schedule accept the plan, but on condition that at least one of the disadvantaged categories also accepted the plan and at least 30 per cent of the aggregate receivables value has accepted the plan;
- each disadvantaged category of receivables that rejected the plan shall be treated correctly and fairly in the plan; and
- receivables that shall be fully repaid within 30 days from the confirmation of the plan or in accordance with the credit or leasing agreements from which they originate shall be deemed non-disadvantaged receivables that have accepted the plan.

We have not come across cases in which reorganisation plans provided for the release from liability of non-debtor parties. Usually, the liability of such persons is requested by creditors in order to ensure a greater recovery of their receivables in instances where the assets of the debtor are insufficient for this purpose and where it may be proven that other parties (such as directors, shareholders, etc) contributed to this insufficiency.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

There is no express provision in the Insolvency Law in this regard. The only expedited and simplified insolvency procedure relates to bankruptcy in certain cases expressly provided by the law (eg, individuals registered as professionals in the Commercial Registry, legal entities wound-up voluntarily before the opening of the insolvency procedure, etc).

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

If no plan is deemed confirmed and the period during which a reorganisation may be proposed elapses, the insolvency judge decides the immediate opening of the bankruptcy and liquidation procedure.

The same is applicable in cases where the debtor does not observe the plan or its activity generates losses and triggers new debts towards

existing creditors. In this case, any creditor party to the insolvency procedure, as well as the judicial receiver, is entitled to request the opening of the bankruptcy procedure.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

Creditors are notified of the opening of insolvency proceedings. Generally, the judicial receiver is entitled to summon a creditors' meeting and serve notifications. At the same time, the publication of the various acts undertaken as part of the insolvency proceedings in the Insolvency Proceedings Bulletin (the Bulletin) replaces the notification requirement regarding the respective act.

Creditors' meetings are called by publication in the Bulletin of the meetings' agenda at least five days before the meeting is held. A creditors' committee is summoned by the judicial receiver or liquidator or by any of its members whenever needed.

Any information regarding the debtor's estate, its assets and claims against it are available to creditors, as they are published in the Bulletin.

The judicial receiver must prepare several reports during the insolvency proceedings, the most important of which is the report on the causes and circumstances that led to the debtor's insolvency and the list of receivables.

The estate's remedies against third parties may be pursued by the judicial receiver as part of its attributions regarding the replenishment of the debtor's estate for the satisfaction of the creditors' receivables (see question 21). A reorganisation plan cannot provide the release of liabilities owed by third parties not linked with the debtor.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

We assume that estate's remedies should be understood as remedies that are available for replenishing the estate of the debtor in order to maximise recovery and realisation.

The judicial receiver has the means of retrieving assets sold or disposed of prior to the opening of insolvency proceedings for the debtor's estate (such as invalidation of past transfer acts, claiming of amounts paid fraudulently by the debtor in order to diminish its estate, etc). For more detail, see question 39.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

A creditors' meeting and committee can be formed, the latter of which, where applicable, aims to provide creditors with centralised decision-making bodies to match those of the debtor, in order to monitor the course of the proceedings and to steer it toward the best interest of the creditors.

The creditors' committee may be designated by the insolvency judge by reference to the number of creditors who are parties to the procedure. It may have either three or five members, selected from among the creditors with voting rights, those having secured receivables, as well as those having the highest receivables owed to the state's budget and unsecured receivables. Creditors may and in practice usually do retain legal advisers. Any costs (including costs associated with their advisers) are borne by the debtor and will be recovered following the completion of the insolvency procedure.

The creditors' committee is responsible for analysing the debtor's situation and making recommendations with respect to the debtor's activity, negotiating with the judicial receiver or liquidator, reviewing their reports, etc.

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**Insolvency of corporate groups**

- 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

In case of the opening of insolvency proceedings against members of a group of companies, the insolvency proceedings may be combined for administrative purposes before the competent tribunal.

There are no provisions in the Insolvency Law allowing assets and liabilities of companies within a group to be pooled for distribution purposes. Each member of a group is normally regarded as a separate entity. However, all economical decisions taken during the insolvency proceedings are governed by opportunity and the scope of protecting the creditors' interests.

Regarding the transfer of assets of a member of the group, the Insolvency Law stipulates that actions to annul the transfer of property rights may be filed against a member of the group (relevant with respect to transfer of assets between group members).

However, Romanian legislation stipulates that a member of the group may grant a loan to another member of the group undergoing insolvency proceedings, with the consent of the creditors' committee, in order to support the activity of the debtor, within the observation period or to support the reorganisation plan.

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**Appeals**

- 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

As a general rule, all decisions issued by the insolvency judge are subject to appeal before the Court of Appeal. There are no specific requirements for filing an appeal. However, in contrast with the regular procedure, the appeals have to be filed within shorter deadlines and are assessed in an expeditious manner. In other words, the procedure under the Insolvency Law aims to shorten the length of time required to review and resolve the appeals, so that the duration of the insolvency procedure is not affected by such.

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**Claims**

- 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

Following the opening of the insolvency proceedings, all creditors are notified to file requests for admission of their receivables. The deadline for submitting their requests is established in the notification and cannot exceed 45 days from the opening of the insolvency proceedings. All such receivables are verified by the judicial receiver in order to be or not recorded in the list of receivables. Creditors may appeal against the judicial receiver's decision within seven days from the date when the preliminary receivables list is published in the Bulletin.

There is no express provision regarding the transfer of receivables between creditors, but, as long as these transfers are approved by the judicial receiver, such assignments of receivables during the insolvency proceedings are conceivable.

Claims for contingent or unliquidated damages are accepted to the pool of receivables and registered at the nominal value of such receivables at the date the insolvency proceedings were opened. Receivables benefiting from a preference right are recorded in the list of receivables, up to the market value of the secured assets.

Generally, no interest or similar cost may accrue on receivables that came into existence before the opening of insolvency proceedings, except for the interest related to receivables benefiting from a preference right.

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**Modifying creditors' rights**

- 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

Courts are not allowed to change the rank of a creditor's claim. The rank is established upon perfection of the receivable underlying the respective claim.

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**Priority claims**

- 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Apart from the taxes and other expenses related to the sale of assets, claims of creditors benefiting from preference (such as secured creditors) that came into existence during the insolvency proceedings have priority over the other claims enjoying preference causes and, obviously, over unsecured or unprivileged claims.

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**Employment-related liabilities in restructurings**

- 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

In case of termination of the individual employment agreement, employees may file monetary claims for unpaid wages, wages owed as a consequence of unlawful termination of the individual employment agreement if the legal procedure for termination was not observed by the debtor, and other amounts due deriving from employment relations (eg, such as amounts due in respect to injuries suffered by the employee during working hours).

According to the Insolvency Law, following the opening of the insolvency proceedings of the debtor, the judicial administrator or the judicial liquidator may terminate individual employment agreements, with the legal obligation to grant the employee the prior legal notice period.

In case of termination of individual employment agreements of a large number of employees (collective dismissal), the provisions of the Labour Code must be observed by the debtor as an employer, noting that certain terms are reduced to half given that the debtor is undergoing the insolvency procedure.

Where there are numerous claims for salaries owed to employees, each claim should be analysed separately. However, as per the Insolvency Law, the bankruptcy administrator must register the wage claims in the debtor's receivables list by default.

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**Pension claims**

- 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

The employer must withhold and pay social insurance contributions for the public pension system for each employee. If the debtor has not paid these mandatory contributions, under the insolvency proceedings, such contributions are considered to be budgetary receivables and must be paid to the state budget with priority (fifth-rank priority).

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**Environmental problems and liabilities**

- 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

The company represented by the judicial receiver or liquidator may be held liable for environmental damages. Under the Insolvency Law, the liability of the judicial receiver/liquidator is limited to cases of performing its obligations with bad faith or gross negligence.

Depending on the case, the special receiver may also be held liable for environmental damages. The special receiver may be held liable only in the limit of its powers.

### Update and trends

A new law regarding the insolvency of individuals has recently been adopted and will enter into force at the end of 2016. It comes in response to the significant volume of non-performing loans that has filled the balance sheets of banks as a consequence of the economic and financial crisis.

As far as the Insolvency Law is concerned, although it has only rather recently been enacted, it represents a development of the previous insolvency legislation and includes modifications and fixes that were discovered to be necessary by practice in judicial courts and research by legal scholars. Because of the considerably high number of insolvency cases (for example, in 2013 almost 30,000 new insolvency cases were opened, as opposed to approximately 20,000 in 2014), a series of measures intended to accelerate the proceedings and prevent the rather 'too easy' access to insolvency was implemented. Practitioners and business actors are of the view that the Insolvency Law and the corresponding practice it generates should be a breath of fresh air in the current context (it is estimated that the total number of insolvency cases will actually drop, especially also in the context of the economic recovery and the good macroeconomic figures Romania has been recording in the past couple of years).

### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Upon confirmation of a reorganisation plan, the debtor is discharged of the difference between the value of its debts before the confirmation of the plan and the amount of debt provided in the reorganisation plan.

Upon bankruptcy or liquidation, the situation resulting from the final list of receivables is reinstated. If the amounts realised as part of the liquidation are insufficient to fully cover claims having the same priority, the relevant creditors will be allotted an amount proportional to the percentage that their receivables hold in the respective category.

### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

In case of liquidation, receivables of secured creditors are satisfied first by and mainly through the sale of the respective underlying securing assets. Should the receivables of such secured creditors exceed the funds obtained from the selling of the debtor's assets, such creditors will rank as any other unsecured creditors for the remaining debt.

The distribution of any amounts obtained through the sale of the assets subject to security must be made in the following order:

- taxes, stamp duties and other expenses;
- receivables of secured creditors arising during the insolvency proceedings; and
- receivables of secured creditors.

Following the full satisfaction of the secured creditors' receivables, the unsecured creditors are paid in the following order:

- taxes, stamp duties and other expenses;
- receivables deriving from financing arrangements granted to the debtor within the observation period;
- wages and similar receivables;
- receivables deriving from the continuation of the debtor's activities after the opening of the insolvency proceedings, claims due to contractors as a consequence of the unilateral termination of the agreements by the judicial receiver and claims of third-party acquirers who have returned assets or their value to the debtor's estate as part of the proceedings;
- budgetary receivables (fiscal or tax debt);
- receivables due to third parties having obligations of care or under-age allowances (and similar);
- banking credits, receivables from product deliveries, service provisions or other works, rents; and
- other unsecured and subordinated receivables.

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

As a rule, the judicial receiver or liquidator may file a claim with the annulment of fraudulent acts or operations made by the debtor to the detriment of the creditors' rights within the previous two years.

Among the acts that can be annulled are the following: free transfer acts concluded within the two years preceding the opening of insolvency; operations in which the debtor's obligation manifestly exceeds the corresponding obligation; creation of a preference right for an unsecured receivable within the six months preceding the insolvency, etc.

The main effect of the annulment is that the parties are reinstated in their initial contractual position (eg, the third party acquiring the assets sold by the debtor will have to return the acquired asset or its value at the transfer date, etc).

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

Yes. As mentioned above, the suspect period is generally the two-year period before the opening of the insolvency proceedings. The voidable transactions may be challenged both by the judicial receiver or liquidator and creditors within one year from the expiry of the term for preparation by the judicial receiver of the report regarding the causes and circumstances that led to insolvency, but not later than 16 months from the opening of the proceedings.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The debtor is obliged to file with the competent court a request for opening insolvency proceedings only when it is insolvent. Directors do not have a direct obligation to take action in the event insolvency is imminent. However, as soon as insolvency has become manifest, directors are obliged to file an insolvency request with the competent court.

At the request of the judicial receiver or liquidator, the insolvency judge may order a portion of the debts to be incurred by the company's management (including directors) or by any other person who caused the insolvency situation by actions such as: use of the assets or loans granted to the company for their personal benefit or for the benefit of third parties, etc.

In principle, criminal offences applicable to directors refer to the scenario where the debtor has become insolvent. However, certain criminal offences may apply to directors in general, even before insolvency proceedings have been started (for example, the forging, removal or destruction of the records of the debtor or the concealing of a portion of its assets is deemed to be a criminal offence of fraudulent bankruptcy punished with imprisonment from six months to five years).

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

The law does not expressly provide for the liability of the parent for its subsidiary. The only circumstance in which such liability may become relevant is the one described in question 41, to the extent it is proven that the parent or affiliated entity has caused the insolvency situation.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

No, Romanian legislation does not provide for such kinds of restrictions.

**Creditors' enforcement****44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

If insolvency proceedings have been opened, all creditors must participate in such proceedings in order to satisfy their claims against the debtor. They cannot pursue separate or out-of-court proceedings, as the Romanian insolvency proceedings are collective and unitary.

**Corporate procedures****45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

In Romania, there is no separate concept of 'corporation'. Therefore, the general rules provided by the Insolvency Law apply for all types of Romanian companies.

**Conclusion of case****46 How are liquidation and reorganisation cases formally concluded?**

The bankruptcy proceedings close after the insolvency judge approves the final report drawn up by the liquidator, when all the funds of the debtor are distributed between the creditors and all unclaimed funds are deposited in a bank.

Following a petition submitted by the liquidator, the insolvency judge passes a resolution closing the proceedings and orders deregistration of the debtor from the relevant registries (ie, the Commercial Registry).

**International cases****47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Under Council Regulation (EC) No. 1346/2000 on insolvency proceedings (Regulation 1346/2000), any judgment on opening insolvency proceedings handed down by a court of an EU member state shall be automatically recognised in all other member states with no further formalities and shall produce the same effects in any other member state.

In addition, the UNCITRAL Model Law on Cross-Border Insolvency is incorporated in Romanian legislation. Romanian

legislation provides a procedure for the recognition of foreign judgments. In this respect, a claim for recognition of a foreign judgment must be filed before the Romanian courts.

Under Romanian law, foreign creditors have the same rights with respect to opening and participating in insolvency proceedings initiated under this law as Romanian creditors.

**COMI****48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

In Romania, the test provided in Regulation 1346/2000 is applicable (ie, the COMI is presumed, until contrary evidence is provided, to be the location where the registered office of a company is situated). Criteria that may be taken into account for setting aside this presumption include the location of all the assets of the company or of its employees, the creditors' registered office, etc.

**Cross-border cooperation****49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

Under Romanian law, there are specific procedures for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and foreign insolvency administrators in cross-border insolvencies and restructurings.

Romanian courts may refuse to recognise a foreign insolvency procedure or a foreign judgment adopted in such proceedings, in the event of fraud in the foreign procedure or public policy breaches.

**Cross-border insolvency protocols and joint court hearings****50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

We are unaware of formal arrangements that have been entered into between the Romanian courts and foreign courts to coordinate proceedings. However, Romanian legislation contains provisions addressing cross-border insolvency protocols.

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# Russia

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

In Russian law, the terms ‘bankruptcy’ and ‘insolvency’ are synonymous. Basic legal provisions on bankruptcy are set out in the Civil Code of the Russian Federation (the Civil Code). The main source of legislation on bankruptcy is Federal Law No. 127-FZ on Insolvency (Bankruptcy) of 26 October 2002 (the Bankruptcy Law), which from December 2014 also incorporates the rules on bankruptcies of credit organisations. The other important subordinate legislation is contained in Federal Law No. 83-FZ on Financial Restoration of Agricultural Commodity Producers of 9 July 2002, Federal Law No. 229-FZ on Enforcement Proceedings of 2 October 2007 and Federal Law No. 154-FZ of 29 June 2015 on Regulation of Specific Aspects of Insolvency (Bankruptcy) at the Territories of the Republic of Crimea and Sevastopol as the State of Federal Importance and on Introduction of Changes to Certain Legislative Acts of the Russian Federation (154 Law). 154 Law introduced significant changes to the bankruptcy provisions relating to natural persons, and these changes came into force on 28 September and 1 October 2015. Before 154 Law was enacted, it was not possible to apply bankruptcy procedures to natural persons. Unless specifically stated otherwise, this chapter focuses on matters of companies rather than natural persons.

The Bankruptcy Law sets out that a legal entity or an individual meets the insolvency criteria if such legal entity or individual fails to pay its debts as they fall due for a period of three months starting from the date when the payment obligation fell due (provided that, in the case of an individual, he or she also does not have sufficient assets to perform such obligations, however, according to court practice, this does not apply to individuals registered as individual entrepreneurs). The general rule is that the insolvency case can be opened in relation to a debtor if the above criteria are satisfied and the total amount of the creditors’ claims equals or exceeds 500,000 roubles in relation to individuals or 300,000 roubles in relation to a legal entity.

The law provides for special insolvency criteria and requirements for initiating insolvency proceedings in relation to particular categories of debtors. For example, a financial organisation (including credit organisations) is considered insolvent if:

- it fails to pay its debts (amounting to at least 100,000 roubles) as they fall due for a total period of 14 days;
- it fails to comply with any court decision (arbitration award) on the recovery of funds against the financial organisation within 14 days of such decision coming into force (irrespective of the amount);
- it holds insufficient assets to pay its debts as they would fall due; or
- its financial solvency has not been restored in the course of the activity of the temporary administration.

A strategic company is considered insolvent if it fails to perform its financial obligations for an amount equal to or exceeding 1,000,000 roubles for six months from the date on which such obligations should have been performed.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

There are two types of courts in Russia: civil and arbitrazh (commercial) courts. Insolvency cases fall within the jurisdiction of the commercial courts.

The commercial courts have jurisdiction in relation to all matters arising from or in connection with a bankruptcy case, so there are no restrictions on the matters that the commercial courts may deal with except for criminal proceedings against the management of the debtor, in relation to which civil courts have jurisdiction.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

In principle, bankruptcy proceedings apply to all legal entities and individuals.

The Civil Code expressly excludes the following entities from bankruptcy proceedings:

- treasury enterprises (see question 4); and
- some forms of non-profit organisations, such as institutions, political parties and religious organisations.

A state-owned corporation or state-owned company may only go into insolvency proceedings if expressly provided by the federal law that set up such corporation or company. For instance, corporations such as the state corporation Bank for Development and Foreign Economic Affairs (Vnesheconombank), the state corporation Russian Technologies (Rostec), the state atomic energy corporation Rosatom and state companies such as Russian Automobile Roads (Avtodor) are expressly excluded from bankruptcy proceedings. Additionally, specific federal laws on the foundation and operation of state-owned funds may exclude such funds from bankruptcy proceedings. For example, the legislation that established the Russian Housing Development Foundation and the Advanced Research Foundation expressly excludes bankruptcy proceedings.

The Bankruptcy Law also specifies some types of assets that do not fall within the bankruptcy estate, including:

- (i) assets withdrawn from turnover or limited in their transferability (eg, objects of seaport infrastructure);
- (ii) socially significant facilities and cultural heritage objects;
- (iii) social-use housing facilities;
- (iv) property rights connected with the personality of the debtor (eg, rights to licences to conduct particular activities);
- (v) in the event of a bankruptcy of a professional participant of the securities market, assets of its clients at the special broker, trade, clearing, special depositary, transit, custodian or other accounts and assets that are in trust management for the benefit of the clients of the professional securities market participant;
- (vi) pension savings and pension reserves of private pension funds;
- (vii) mortgage collateral securing obligations of the issuer of mortgage-backed securities;

- (viii) in the event of a bankruptcy of an individual, his or her assets in relation to which an execution cannot be levied (eg, the sole living premises (if not mortgaged), household articles, etc); and
- (ix) in the event of a bankruptcy of a farm, any property owned by the head or members of the farm household or in relation to which it can be proven that such property was not acquired using funds of the farm household.

In relation to most of these assets the law provides special procedures for their transfer from the insolvent debtor to the relevant third parties (for instance, assets indicated under (i) will be returned to their owner, assets specified in (ii) shall be sold by way of a tender on the condition that the successful bidder will be obliged to properly maintain such objects, and the proceeds of such sale will be included in the bankruptcy estate).

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### Public enterprises

#### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

##### Unitary enterprises

State or local authorities may establish companies in the form of a unitary enterprise. Unitary enterprises do not own the assets that are provided to them by the relevant authorities (such assets continue to be owned by the Russian Federation, the subject of the Russian Federation or the municipal unit). The enterprises have either the right of economic management (state enterprises) or the right of operational management (treasury enterprises) in relation to such assets. The second type of right is more limited in nature than the first one.

Under the Civil Code the owner of assets of a state enterprise is not liable for the debt of that enterprise. Conversely, the owner of assets of a treasury enterprise has subsidiary liability for the debts of that enterprise in the event of their insufficiency.

In contrast to treasury enterprises, state enterprises can be subject to bankruptcies in accordance with the Bankruptcy Law and the procedures and the rights of creditors will generally be the same as in insolvencies of companies (see questions 10 and 12). The assets in relation to which the state enterprise has the right of economic management can form part of the bankruptcy estate, provided they are not excluded assets (see question 3).

In relation to treasury enterprises the creditors may try to hold the asset owner liable for the enterprise's debts. This may also be possible in relation to state enterprises provided the bankruptcy of the enterprise was caused by the asset owner.

##### Other government-owned enterprises

As stated above, state-owned corporations, companies and funds are not subject to insolvency proceedings (see question 3). They can be liquidated based on special federal laws providing for the procedure of such liquidation. The creditors of such companies can bring claims against them in the ordinary course. In the event of insufficiency of assets to satisfy such claims the creditors will not have any additional remedies.

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### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Generally, no special legislation has been enacted in Russia to deal with the financial difficulties of institutions that are considered 'too big to fail', but the Bankruptcy Law sets out certain specific rules with respect to bankruptcy procedures in relation to strategic companies, natural monopolies and city-forming enterprises. Most of these specific rules aim to provide more possibilities to restore the financial solvency of such companies. For instance, in the course of bankruptcy proceedings of city-forming enterprises the respective local or state authorities may ask the court (i) to apply external administration in relation to the debtor, or (ii) to prolong the term of the financial restoration or external administration (but not more than by one year), provided in both cases that a suretyship securing the obligations of the debtor will be issued by such authorities.

Additionally, there are certain entities to which the bankruptcy proceedings set out in the Bankruptcy Law do not apply (see question 1).

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### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

The principal type of security taken on immoveable property is a mortgage. A mortgage charges the debtor's title to the property and, generally, prevents its transfer without the mortgagee's consent. A mortgage does not involve the transfer of ownership of the property by the mortgagor to the mortgagee. When the liquidation of a mortgagor of immoveable property is initiated, the charge created by the mortgage ceases to exist but the mortgagee has a right to be paid his or her debt in priority to unsecured creditors from the proceeds of sale of the mortgaged property. Under the Bankruptcy Law the mortgagee is entitled to receive up to 70 or 80 per cent (in any case not more than the total indebtedness under the secured obligation) from the proceeds of sale of the mortgaged property.

A mortgage is subject to state registration and the payment of a state fee of 4,000 roubles by legal entities or 1,000 roubles by individuals.

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### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The principal type of security taken on moveable property is a pledge. A pledge charges the title to the moveable property and prevents its transfer without the pledgee's consent. A pledge does not involve the transfer of ownership of the property by the pledgor to the pledgee. When the liquidation of an owner or pledgor of moveables is initiated, the charge created by the pledge ceases to exist but the pledgee has a right to be paid his or her debt in priority from the proceeds of sale of the pledged moveables. Under the Bankruptcy Law the pledgee is entitled to receive up to 70 or 80 per cent, but not more than the total indebtedness under the secured obligation, of the proceeds of sale of the pledged property. In bankruptcy proceedings, the priority right of the pledgee generally ranks third.

The Civil Code provides sellers of goods that are purchased on credit with a mandatory pledge over the goods transferred to the debtor until they are paid for, unless otherwise agreed by contract.

Although there is no registration requirement, pledges on moveable property may be registered by a notary in the register of pledge notices upon application of the pledgor or pledgee.

Both mortgages (as above) and pledges may be provided to a creditor not only by the principal debtor but also by a third party. Creditors can also secure their interest with a lien. A lien gives a creditor the right to retain the possession of a debtor's assets until the debt has been paid. Liens are created by law and are rarely contracted upon in Russia. However, the effects of a lien under bankruptcy proceedings are unclear.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Generally, claims of unsecured creditors rank third and they are satisfied only after all first and second-ranking creditors are paid in full (see question 33 with respect to ranking of creditors' claims). In practice the recovery rate in relation to the third-ranking creditors is very low.

The process is often difficult and time-consuming because (i) the courts' verification of a claim may take several months if the claim is not confirmed by a court judgment or arbitral award and (ii) additional time may be required to identify the debtor's assets in cases where they have been siphoned off. It is not uncommon for insolvency cases to continue for two or more years.

During bankruptcy proceedings creditors can apply for interim measures generally available in court proceedings (for instance, freezing orders, transfer of assets to be kept by third parties etc). Creditors can also apply for specific interim measures set out in the Bankruptcy Law, such as a prohibition on the insolvent company from entering into certain transactions without the consent of the temporary administrator during the supervision stage of bankruptcy proceedings. No interim measures may be obtained once the liquidation has begun.

Under the Bankruptcy Law, foreign creditors have the same status as Russian creditors, unless otherwise provided for in an applicable international treaty.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A solvent company can be liquidated under a voluntary corporate procedure. The beginning of a voluntary liquidation does not trigger a moratorium on claims against the company. See questions 45 and 46 with respect to corporate procedure for the liquidation of a company that is solvent.

A company that is insolvent can itself initiate bankruptcy proceedings leading to its liquidation by filing a bankruptcy petition with the court pursuant to a decision of the company's authorised body. The debtor is entitled to file a bankruptcy petition only if it shows an inability to meet its debts or to pay tax and other amounts because of state organisations such as social levies (the compulsory payment) as they become due.

The effects of liquidation are the same, whether the liquidation was initiated by the debtor or by any other party entitled to initiate it (see below).

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

There is a difference between involuntary liquidation of a solvent company and bankruptcy proceedings.

##### Solvent company – involuntary liquidation

A solvent company can be liquidated pursuant to an involuntary liquidation procedure in several cases provided by Russian law, for instance:

- if registration of the company has been declared invalid, including in case of non-remediable gross violations of law in the process of the company's foundation;
- if the company has conducted any activity without necessary regulatory licence or approval or in absence of membership of the relevant self-regulating organisation or of certificate on admission to a particular type of activity issued by the relevant self-regulating organisation (if such a certificate is required by law);
- if the company has conducted any activity that is prohibited by law or violates the Constitution of the Russian Federation or other laws (provided, in the case of other laws, that the violation is gross or repeated);
- if a social organisation, a charity or other fund or a religious organisation repeatedly conducts activity contradicting its statutory purposes; and
- if it becomes impossible to achieve the aims for which the company was founded if conducting activity by such company becomes impossible or materially complicated.

Such involuntary liquidation could be initiated by the competent state or municipal authorities or, in the case of impossibility to achieve the company's aims as specified above, by a founder or shareholder of the company. Creditors cannot validly file a request to place a debtor in involuntary liquidation unless the debtor is deemed to be absent (see below).

An involuntary liquidation procedure may be initiated in relation to a solvent credit organisation at the request of the Central Bank within 15 days of the revocation of the banking licence of such credit organisation.

##### Insolvent company – bankruptcy proceedings

Creditors can file a bankruptcy petition that may lead to liquidation if the company is deemed irremediably insolvent. In reviewing the bankruptcy petition, the court must determine whether or not the company is insolvent. If the court determines that the company is not insolvent, it will dismiss the bankruptcy petition.

A company is deemed insolvent, and so subject to bankruptcy proceedings initiated by a party other than the debtor itself, if it is not able to satisfy its monetary obligations to creditors or has failed to make compulsory payments. The court will only allow proceedings to be started in relation to a company if:

- the sum of the unsatisfied claims or the compulsory payments outstanding exceeds a certain amount (the minimum unsatisfied claims); and
- the minimum unsatisfied claims are confirmed by a judgment or an arbitral award (except in relation to the compulsory payments and claims of credit organisations as stated below). Also see question 1 regarding insolvency criteria and requirements that should be met in order to initiate insolvency proceedings against a debtor.

Claims in relation to the compulsory payments are relevant to initiate the bankruptcy procedure if they are confirmed by the decisions of tax or customs authorities on debt recovery. Such claims do not necessarily need to be confirmed by a judgment. They must have been outstanding for at least 30 days after the decision to collect the indebtedness has been taken by the authorities.

Claims of credit organisations, which are relevant to initiate the bankruptcy procedure, do not need to be confirmed by a judgment. Credit organisations are entitled to bring a bankruptcy petition against a debtor, provided the insolvency criteria are met.

##### Supervision stage

If the court decides that the company is insolvent, it will place the debtor under supervision and appoint a supervisor. The court may decide to liquidate a company after the supervision stage is commenced and when it is satisfied that the company's solvency cannot be restored.

The main functions of the supervisor are to identify the creditors, to analyse the financial status of the company and to convene and conduct the first creditors' meeting. The first creditors' meeting must be held at least 10 days prior to the end of the supervision stage. At this meeting the creditors may decide whether they will request the court to commence financial restoration, external administration or liquidation of the company. Subject to some exceptions, the court must follow the decision of the creditors' meeting.

Upon commencing the supervision stage, a creditor can stay its monetary claim against the debtor and submit its claim within the procedure established by the Bankruptcy Law.

The supervision stage must be completed within seven months from the date when a bankruptcy petition was filed.

##### Financial restoration and external administration

If, on completion of the supervision stage, the court considers that the debtor's solvency can be restored, it may place the company into financial restoration or external administration. Both stages together may last for a maximum of two years (see question 12).

##### Bankruptcy proceedings

When the court decides that the company's solvency cannot be restored, it will order bankruptcy proceedings and appoint a bankruptcy trustee.

The main effects of the start of bankruptcy proceedings are that the business of the company ceases except to the extent that is necessary to complete the bankruptcy proceedings, monetary obligations (including the compulsory payments) of the company become due and no forfeits or interest accrue on its debts.

Bankruptcy proceedings must be carried out over a period not exceeding 12 months. The bankruptcy trustee replaces the management in its duties and has the authority to deal with the company's assets to satisfy the creditors' claims. All assets of the company available at the start of bankruptcy proceedings must be evaluated and, where possible, sold.

In some cases, the return to external administration during bankruptcy proceedings is allowed (see also question 12).

##### Bankruptcy of an absent debtor

The Bankruptcy Law sets out a simplified bankruptcy procedure for absent debtors. The procedure applies to a company whose business is no longer operating, whose management cannot be contacted, whose assets are obviously not sufficient to cover court costs, whose bank accounts show that no transaction was carried out or there is other evidence of an absence of business activity for at least 12 months before the bankruptcy petition was filed.

In these cases, a bankruptcy petition may be filed without regard to the minimum threshold requirement. Within one month of the bankruptcy petition being filed, the court must declare the company

bankrupt and order bankruptcy proceedings. All creditors will be notified of the start of the bankruptcy proceedings and will have the right to submit their claims directly to the bankruptcy trustee within one month. The court may terminate the simplified bankruptcy procedure if the bankruptcy trustee locates its assets. This makes the debtor subject to the general bankruptcy procedure described above and in question 12.

#### **Strike-off of dormant companies**

Russian law provides a simplified liquidation procedure for a 'dormant company' (a company that has not submitted its financial reports and has not performed any bank account operations within the previous 12 months). A dormant company may be excluded from the state register of legal entities by the registration authorities without any liquidation procedure, provided that no creditors' claims are submitted against such company within three months of publication by the registration authorities of the relevant announcement. If any creditors' claims are submitted the company must be liquidated in accordance with the usual liquidation procedure set out above.

#### **Bankruptcy of credit organisations**

In accordance with the Bankruptcy Law, a request for bankruptcy of a credit organisation can be filed with the court only following the revocation by the Central Bank of that credit organisation's banking licence. The debtor, creditors and other authorised bodies can file a request with the Central Bank to revoke the banking licence.

If the Central Bank revokes the banking licence, it must appoint a temporary administration over that credit organisation. Temporary administration of a credit organisation is a measure to determine the financial condition of the credit organisation, assess and preserve its assets and supervise the activities of the credit organisation by replacing or limiting the functions of its executive and management bodies. A temporary administration in relation to a credit organisation can last for a maximum period of six months.

Following the temporary administration of the credit organisation, a credit organisation can only enter liquidation. Financial restoration and external administration mentioned above are not available to credit organisations.

The Bankruptcy Law also sets out a simplified bankruptcy procedure for absent credit organisations.

#### **Bankruptcy of financial organisations**

Subject to rules on the insolvency of credit organisations, the Bankruptcy Law also provides some specific rules with respect to insolvencies of financial organisations (credit organisations, insurers, professional participants of capital markets, management companies of investment funds, unit investment funds and private pension funds, clearing organisations, trade institutions (stock exchanges), consumer credit cooperatives and 'microfinancial organisations'). Generally, these rules are intended to reveal any weakening in the organisation's financial standing to the regulator.

If the regulator detects a weakening of the organisation's financial standing, it could (and in certain cases must) appoint a temporary administrator with the purpose of applying bankruptcy prevention measures, protecting the organisation's assets and controlling the performance of the financial organisation by a financial standing restoration plan, etc. The maximum term of the temporary administrator in relation to the bankruptcy of a financial organisation is nine months. If the temporary administrator was appointed and finds that the financial standing of the organisation cannot be restored, the financial organisation will initiate bankruptcy proceedings.

A financial organisation cannot enter into financial restoration or external administration.

#### **Bankruptcy of special purpose vehicles and mortgage collateral agents**

The Bankruptcy Law sets out special rules regarding bankruptcy proceedings of special purpose vehicles (SPVs). Russian law specifies two types of SPVs:

- SPVs whose purpose is to issue bonds secured by a pledge of monetary claims under various financial agreements and acquisition of such claims; and

- SPVs whose purpose is to finance a long-term investment project by way of acquisition of claims arising in the course of the project, assets necessary to carry out the project and assets necessary or connected with the performance of the project and to issue bonds secured by pledge of the said claims and assets.

The supervision, financial restoration and external administration mentioned above and set out by the Bankruptcy Law are not applied to SPVs and mortgage collateral agents.

Generally, the rules on bankruptcy of SPVs and mortgage collateral agents reflect the specifics of the debtors, for example, the holders of bonds issued by the SPV act in insolvency process through their representative (who can file a bankruptcy petition based on the minutes of the bond holders meeting, for instance), the debtor and the creditors are restricted in the ability to file a bankruptcy petition if under the agreement with such creditors or under the SPV's charter such filing is conditional upon occurrence of particular events or dates, the assets securing the obligations of the SPV under the bonds could be transferred to another SPV provided the latter accepts all rights and obligations of the transferor as bond issuer.

#### **Bankruptcy of natural monopolies and strategic companies**

There are specific rules dealing with the commencement of insolvency proceedings in relation to natural monopolies and strategic companies that are, in general, directed towards making a bankruptcy petition against such organisations less likely to succeed.

### **Voluntary reorganisations**

#### **11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

Generally, there is no formal legal process for a voluntary reorganisation initiated by a debtor on the verge of insolvency. The debtor, however, is entitled to request a creditors' meeting to introduce financial restoration during the supervision stage (see question 10).

A solvent company may request a restructuring of its debts owed to the state. Requests are generally made to the finance and tax ministries. Restructuring may grant a company more time to repay or write off part of its debt. A company may also benefit from state grants, subventions and credits.

An insolvent company may be subject to bankruptcy proceedings that may lead to a composition or reorganisation (financial restoration or external administration (see question 12)).

Any shareholder or participant of an insolvent company or any third party can, at any time before the end of bankruptcy proceedings, offer to pay all of the company's debts to prevent the ultimate liquidation of the company. This may be done either by paying the creditors directly or providing the debtor with sufficient funds to do so.

### **Involuntary reorganisations**

#### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

Creditors cannot file a request to place a debtor in involuntary reorganisation. Creditors may file a bankruptcy petition to initiate bankruptcy proceedings that may lead to financial restoration, external administration or composition.

#### **Financial restoration**

During the supervision stage the debtor, its shareholders or participants or any third party (with the agreement of the debtor) – each, in these circumstances, referred to as a requesting party – may ask the creditors' meeting to decide to commence a financial restoration. The financial restoration is generally ordered by the court based on the decision of the creditors' meeting.

Financial restoration is aimed towards the repayment of debts, in accordance with a plan and payment schedule, while preserving the debtor as a going concern. It is generally up to the requesting party to secure the repayment of debts by the debtor – the assets of the debtor itself cannot be used to create such a security. If the debts of the debtor are repaid, the court terminates the bankruptcy procedure.

### External administration

If, at the end of the supervision stage, the creditors do not request that the court orders a financial restoration or, if at the end of the financial restoration, the company's solvency is not restored, the court may decide to place the company into external administration.

Once external administration is entered the management of the company is taken over by an external administrator and a moratorium is imposed on the payment of debts (see question 15). With certain exceptions, the external administrator has authority to deal with all of the company's assets to restore the company's solvency. The external administrator also prepares a reorganisation plan for the creditors to adopt.

If the company's solvency is restored during the external administration, the court will terminate the bankruptcy proceedings.

### Composition

A composition may be started between the debtor and the creditors (third parties may also participate in the composition) at any time during bankruptcy proceedings, subject to the full repayment of debts of the first and second-ranking creditors (see question 33). A composition is an agreement between the debtor and all third-ranking creditors, confirmed by the court, to settle the insolvent company's debts. The composition must be approved at the creditors' meeting by a simple majority of all third-ranking creditors and is subject to the unanimous consent of all secured creditors. Third parties are also allowed to participate in a composition and may secure the debtor's obligations.

The Bankruptcy Law provides a mechanism that may give effect to a composition, even if it is opposed by some creditors, as creditors who voted in favour of the composition are entitled to satisfy the claims of the creditors who voted against it.

A composition may, subject to the individual creditor's consent, include the deferral of payments to the individual creditor, payment of the debt by instalments or discounting, refinancing or sale of debts due to the creditor and debt-for-equity swaps, as well as some other measures. Unless otherwise agreed upon in a composition, any pledge or mortgage does not cease to be effective and if the debtor fails to perform its obligations under the composition towards the relevant secured creditor, such creditor may be paid from the proceeds of the sale of the security as the mortgage or pledge allows.

When the composition is approved by the court, the bankruptcy proceedings are terminated and management of the company will revert to its directors from the insolvency office holder and, provided that debts are repaid as provided for in the composition, business is conducted as before the bankruptcy proceedings.

A composition approved by the court cannot be unilaterally refused or terminated by either party. However, the court may be requested to terminate or invalidate the composition. If the composition is invalidated or terminated by the court, the bankruptcy proceedings recommence but any claims already satisfied during the composition are not unbound. The court may terminate the composition as regards to all creditors.

If the debtor fails to perform its obligations under the composition, creditors are entitled to apply to court for receipt of the enforcement order on recovery of outstanding claims without requesting termination of the composition.

### Involuntary reorganisation of a credit or financial organisation

Financial restoration, external administration and composition are not applicable to credit organisations (see question 11). Instead, the Bankruptcy Law set out specific procedures that apply only to credit organisations: financial rehabilitation, appointment of temporary administration and reorganisation. These procedures may only be entered into by credit organisations outside of court bankruptcy proceedings. Financial rehabilitation must be entered into prior to the bank licence revocation.

Financial restoration and external administration are not available for financial organisations (see question 11). If the temporary administrator decides that the solvency of a financial organisation could be restored, he could institute certain bankruptcy prevention measures (including reorganisation). The Bankruptcy Law does not provide for an exhaustive list of such measures.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

An insolvent company is obliged to file a bankruptcy petition within one month of finding that it is unable to pay its debts as they fall due. If the debtor's management fails to file a bankruptcy petition during this period, it can be held liable for the company's debts, liabilities or other obligations that arose after the date when the bankruptcy petition should have been filed.

Although Russian law does not expressly specify the consequences of carrying on the business of an insolvent company it should be also noted that:

- transactions entered into by the debtor in breach of the creditors' interests or transactions that are not at an arms-length basis could be invalidated in any further bankruptcy proceedings; and
- persons controlling the debtor (see question 42) are, prima facie, jointly liable for the debts of the company, so if an insolvent company continues to trade without filing a bankruptcy petition it could increase the liability of the said persons.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

Subject to some exceptions, reorganisations outside of bankruptcy proceedings (see question 11) do not impose restrictions on the company's business activities. However, the company's business during the supervision, financial restoration and external administration stages of bankruptcy proceedings is subject to some restrictions.

As a general rule, the claims of creditors who supply goods or services to the debtor arising after the insolvency proceedings have been initiated are not included on the register of creditors' claims and such creditors do not participate in the bankruptcy proceedings. Such claims rank ahead of other claims (see also question 33).

### Supervision and financial restoration

During the supervision and financial restoration stages, the management of the company remains in place and continues in its duties. However, in each case the court appoints an insolvency office holder to supervise the management and to limit, to some extent, the management's authority. For example, the management will have no authority to make decisions on the payment of dividends. All transactions involving acquisition or disposal of immovables or moveables of a value exceeding 5 per cent of the company's assets are subject to the prior consent of the supervisor in supervision or the creditors' meeting in financial restoration.

Financial restoration, however, imposes more restrictions on the company's business. In particular, any transactions involving the acquisition or disposal of immovables or moveables and assignment of claims are subject to the prior consent of the insolvency office holder.

### External administration

Once the company is placed in external administration, the external administrator replaces the management of the company. However, shareholders or the board of directors may still take decisions to try to return the company to solvency, such as increasing the charter capital by the placement of additional ordinary shares. The external administrator has authority to deal with all the company's assets but his or her powers are restricted. For example, any major or interested-party transactions concluded by the external administrator are generally subject to the prior consent of a creditors' meeting (creditors' committee). As a general rule, the external administrator can also disclaim the debtor's contractual obligations within three months of its appointment (refer to question 10).

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**Stays of proceedings and moratoria**


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- 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

**Supervision and financial restoration**

There is no moratorium as such during the supervision and the financial restoration stages. However, creditors are allowed to request that the court suspend legal proceedings against the debtor's assets at any stage in the bankruptcy proceedings.

During the supervision stage or financial restoration, legal proceedings against the debtor can continue but any enforcement of claims related to debts that were due before the supervision stage or financial restoration are stayed. In the supervision stage, the debtor may repay its debts subject to the ranking of creditors. In the financial restoration stage, the debtor must repay its debts in accordance with a plan and a payment schedule. Generally, while penalties will not accrue on these debts during the financial restoration stage, interest will continue to accrue.

**External administration**

At the external administration stage, a moratorium is introduced on the payment of debts that became due before the external administration. Legal proceedings against the debtor can continue but enforcement of claims related to debts that were due before the external administration is stayed. In general, there are no penalties, but interest on debts continues to accrue. The external administrator usually repays debts incurred during the external administration and debts connected with personal injury, employees' and copyright fee claims. Payment of debts incurred before the external administration, but that became due after that time is not prohibited but may be subject to challenge on the grounds specified in the Bankruptcy Law (for instance, preferential treatment of creditors).

**Bankruptcy proceedings**

At the bankruptcy proceeding stage, legal proceedings against the debtor can continue. No claims against the company's assets may be enforced. All the company's obligations become due and debts may only be repaid subject to the priority rules established by the Bankruptcy Law. No interest or penalties can accrue.

After termination of the bankruptcy proceedings, no prohibitions apply. The Bankruptcy Law does not contain provisions applicable to obtaining relief from the prohibition of execution. However, as mentioned in question 2, some types of claims may be brought outside bankruptcy proceedings.

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**Post-filing credit**


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- 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

Pursuant to the Bankruptcy Law, the insolvent company may obtain loans or credits. However, obtaining a loan or a credit is subject to the prior consent of an insolvency office holder or the creditors' meeting. Any claims that arise from such loans or credits rank ahead of all other claims (see question 32).

An insolvent company is not prevented, at any stage of the bankruptcy proceedings, from pledging its assets to secure the repayment of such loans or credits. Pledging of the debtor's assets is subject to the prior consent of the insolvency office holder or the creditors' meeting (committee).

Certain restrictions apply at the financial restoration stage and the assets of a debtor cannot be pledged to secure repayment of loans or credits in accordance with the payment schedule (see question 12). However, third parties are allowed to secure the repayment of loans or credits by the debtor in accordance with the payment schedule.

The Civil Code gives a lender the right to refuse a borrower to draw down (in full or in part) under an executed loan agreement if it is evident that the loan will not be repaid.

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**Set-off and netting**


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- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

Creditors are allowed to exercise the rights of set-off or netting during the supervision, financial restoration and bankruptcy proceedings stages to the extent that these procedures comply with the order of priority of the creditors' claims (see question 32). It is not clear whether the rights of set-off or netting can be exercised in the external administration.

Creditors are not allowed to exercise the rights of set-off during the bankruptcy proceedings of a credit organisation.

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**Sale of assets**


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- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

The sale of pledged or mortgaged property during bankruptcy proceedings will generally be subject to the prior consent of the relevant secured creditor.

The sale of immovables and businesses is subject to state registration and the payment of a state fee (22,000 roubles by legal entities or 2,000 roubles by individuals for immovables and up to 60,000 roubles for the sale of a business).

In accordance with general provisions of the Civil Code, assets should be transferred to the purchaser free of any third-party rights, except where the purchaser consents to purchase the assets encumbered with rights of third parties or where the law expressly provides that such third-party rights shall continue to exist (ie, the general rule that pledges do not terminate when assets are transferred). The Bankruptcy Law does not provide any special provisions with respect to passing liabilities with the assets acquired by the purchaser, except for sale of the entire business of a debtor in external administration or bankruptcy proceedings. In these circumstances payment obligations are generally not included in the business, save for obligations of a debtor that have arisen after filing a bankruptcy petition with the court.

The Bankruptcy Law does not allow 'stalking horse' bids or credit bidding.

**Financial restoration**

The Bankruptcy Law does not establish special rules for the sale of some assets or the entire business of the debtor at the financial restoration stage. Subject to the terms of the financial restoration plan or the relevant consent of the insolvency office holder (see question 14), the debtor is free to dispose of its assets.

**External administration**

Subject to the terms of the external administration plan, the external administrator may sell some assets or the entire business of the debtor. The relevant assets are first evaluated and then sold by the external administrator through a public auction. The starting price of the sale of the debtor's assets or business is established by the creditors' meeting on the basis of a market price determined by an independent appraiser.

Assets of a value less than 100,000 roubles are not subject to compulsory sale through a public auction and may be sold pursuant to the external administration plan. However, where only certain assets are being sold, this must not make it impossible for the debtor to conduct its business activities. Some assets (such as precious metals and stones) must be sold by tender reserved for participants who are specially licensed by the state (closed tender).

**Composition**

The debtor may sell some assets, or its entire business, as agreed with the creditors in a composition (see question 12). The Bankruptcy Law does not require that the assets be sold by public auction.

### Bankruptcy proceedings (liquidation)

The bankruptcy trustee evaluates all assets of the company available at the start of the bankruptcy proceedings (see question 10) and, where possible, sells them separately or as an entire business. The procedure for sales is similar to that conducted at the external administration stage.

### Intellectual property assets in insolvencies

**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

Under Russian law, the licensor or owner of IP is generally able to terminate the counterparty's right to use the IP if the counterparty enters into insolvency proceedings. Such termination is possible only with a court order if the opening of the insolvency proceeding regarding the IP holder's counterparty is recognised by the court to be an essential change of circumstances. Pursuant to Russian law, the change in the circumstances will be recognised as essential if the counterparty has changed to such an extent that, had the parties been aware of the change of circumstances at the time of the contract, the contract would not have been concluded by them or would have been concluded on different terms.

An agreement regarding the use of IP can also be terminated by the parties without a court order where the agreement expressly provides for such termination.

### Personal data in insolvencies

**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Russian bankruptcy law does not provide for specific rules in relation to personal or customer data use or transfer in the course of reorganisations.

General restrictions could apply in this case, for example, prohibition on disclosing any personal data of a company's counterparties or clients based on the contracts with such counterparties or clients.

In relation to the personal data of individuals (ie, any information relating to the individual that may be directly or indirectly identified based on this information) Russian law sets out that, as a general rule, they can be processed subject to the respective individual's prior consent. Personal data processing means any actions in relation to the personal data, including, but not limited to, collection, recording, storage, updating, changing and transfer (including cross-boundary transfer and transfer for commercial purposes of the personal data).

Therefore, generally, an insolvent company may transfer personal data of its employees and customers to a third party (eg, to a purchaser) subject to prior written consent of the respective individuals. The consent on personal data transfer should include, inter alia, an exhaustive list of companies and individuals that will receive the personal data, particular information that will be transferred and purposes of such transfer. The law also provides that in some cases such consent is not required, for instance, if personal data processing is needed for court decision enforcement (so this could be relevant for insolvency cases).

### Rejection and disclaimer of contracts in reorganisations

**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

#### External administration

The Bankruptcy Law provides special grounds for a debtor in external administration to refuse to perform contracts. A debtor may only refuse to perform contracts or other transactions if it has not begun performance, and if performance would hinder the debtor's financial

rehabilitation or if performance, compared with similar transactions entered into under similar circumstances, would cause losses for the debtor. The external administrator may refuse to perform the contract within three months of the company going into external administration. The external administrator must give notice to the counterparty to the agreement of this intention. An agreement is considered terminated from the date on which this notice is given. The counterparty to the agreement may then seek compensation for losses incurred as a result of the debtor's refusal to perform the agreement.

A debtor may not refuse to perform contractual obligations in relation to agreements entered into during the supervision stage or financial restoration if such agreements were pursuant to the Bankruptcy Law.

### Bankruptcy proceedings

A debtor may refuse to perform contracts or other transactions during bankruptcy proceedings and the counterparty can claim compensation for any loss suffered as a result of the debtor's refusal.

### Credit organisation

Such refusal is also possible if the debtor is a credit organisation. In this event, the insolvency office holder appointed in relation to the credit organisation may refuse performance of transactions that are not performed by the parties in full or in part, if performance by the debtor of such transactions, compared with similar transactions entered into under similar circumstances, causes losses for the debtor.

### Breach after insolvency

If a debtor breaches the contract after the insolvency proceeding is opened, the creditor under the contract can submit a claim in accordance with the procedures set out by the Bankruptcy Law. Generally, any claim of the creditor for payment by the debtor as liability for breach of the contract follow the qualification of the creditor's claims under the contract (if such creditor's claims under the contract are subject to inclusion on the register of creditor's claim, the claims for breach of the contract should be included in the register as well). However, in accordance with the court's interpretation if the creditor performed its obligations under the contract before the insolvency proceeding is opened and then such contract terminated as a result of non-performance by the debtor, the claims of the creditor in such a case should be included in the register of creditors' claims.

### Arbitration processes in insolvency cases

**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

As stated above, the commercial courts have jurisdiction with respect to insolvency cases (see question 2). Insolvency cases are therefore generally not arbitrable.

However, the commercial court will not interfere in arbitration initiated by any person against the debtor, before commencement of bankruptcy proceedings, although any award will not be enforceable unless it is included on the register of creditors' claims. After initiation of the insolvency proceedings, a creditor cannot bring a monetary claim in arbitration.

Generally, insolvency law does not limit the right of the debtor (its insolvency office holder) to bring any actions and sustain them, so arbitration proceedings could continue.

### Successful reorganisations

**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

#### Financial restoration

The financial restoration plan include measures to pay creditors' claims in accordance with the payment schedule set out in the plan. Specific measures are not set out in the Bankruptcy Law. The financial restoration

plan and the payment schedule must be approved at the creditors' meeting. In addition, the payment schedule must be approved by the court.

If, at any time before the end of the financial restoration, the debtor duly repays all debts, the bankruptcy proceedings will terminate. If the debtor failed to perform its obligations in accordance with the payment schedule, the parties that provided security for the debtor's obligations under the payment schedule (the requesting parties) are obliged to satisfy the creditors' claims. If the requesting parties satisfy the creditors' claims, the bankruptcy proceedings may terminate (the requesting parties will be entitled to submit their claims to the debtor outside the bankruptcy procedure) or the bankruptcy procedure may continue (the requesting parties will be entitled to submit their claims to the debtor during the bankruptcy procedure stage as third-ranking creditors).

One month before the financial restoration is completed, the debtor must prepare a report on the results of the financial restoration. The Bankruptcy Law does not require the report to be approved; it will only be considered by the administrator, at the creditors' meeting and by the court. If the court decides the debts have been repaid in full, the bankruptcy procedure terminates.

Settlement of creditors' claims during financial restoration is conducted in accordance with the payment schedule. The payment schedule should provide for the proportional settlement of creditors' claims, in accordance with the rank of creditors' claims established by the Bankruptcy Law (see question 33). Therefore, no releases in favour of creditors may be created by the payment schedule or the financial restoration plan; however, the Bankruptcy Law establishes priority of settlement of creditors' claims filed during the supervision stage (ie, included into the payment schedule) over claims filed during the financial restoration stage. Claims filed during the financial restoration stage are not included in the payment schedule and are satisfied upon settlement of claims included in the payment schedule.

#### External administration

The reorganisation plan should contain appropriate measures to restore the company's solvency, such as:

- the sale of the company's assets;
- the sale of the business;
- the assignment of the debtor's claims (the sale of such claims must be through a public auction with the consent of the creditors' meeting (creditors' committee));
- the recovery of receivables;
- the performance of the debtor's obligations by its shareholders, participants or any third parties;
- the placement of additional ordinary shares under a closed subscription; or
- the establishment of open-stock companies on the basis of the debtor's assets.

Such measures are not exhaustively set out in the Bankruptcy Law.

The Bankruptcy Law does not state that the reorganisation plan can release the non-debtor parties from liability. Having regard to the fact that the reorganisation plan provides for measures to restore the debtor's solvency, such release may be considered contrary to the purpose of the external administration and in breach of the creditors' rights, which may lead to the invalidation of the reorganisation plan.

Within one month of his or her appointment, the external administrator must submit a reorganisation plan to the creditors' meeting for approval. The plan must also be submitted to the court.

The external administrator must submit a report to the creditors at the end of the external administration (when the plan has been implemented or in the event of early termination of the external administration) or if the debtor has accumulated funds sufficient to satisfy all creditors' claims. The creditors' meeting must consider the report and decide whether the company's solvency has been restored and then submit the report and its decision to the court. If the creditors have agreed that solvency has been restored, the court approves the report and terminates the bankruptcy proceedings.

Creditors are allowed to submit their claims at any time during the external administration. Such claims are included in the register of creditors' claims and should be settled in accordance with the rank of creditor's claims established by the Bankruptcy Law (see question 33). Therefore, no releases in favour of creditors may be created by the reorganisation plan.

#### Expedited reorganisations

##### 24 Do procedures exist for expedited reorganisations?

There are no procedures for expedited financial restoration or external administration but, according to the Civil Code, it is possible to combine several types of reorganisation (transformation and merger for instance) into one procedure.

#### Unsuccessful reorganisations

##### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

###### Financial restoration

If the debtor fails to repay its debts in accordance with the payment schedule and the parties that provided security for the debtor's obligations under the payment schedule fail to satisfy the creditors' claims, the schedule can be amended subject to the consent of the creditors. If the creditors do not agree to amend the payment schedule, the court is likely to commence external administration or bankruptcy proceedings.

If the administrator considers that the debtor's report on the results of the financial restoration does not show that the creditors' claims have been satisfied, the administrator will convene a creditors' meeting. The creditors may then decide to put the debtor into external administration or commence bankruptcy proceedings. Generally, the court will follow the decision of the creditors' meeting.

###### External administration

If the creditors do not approve the reorganisation plan or the approved reorganisation plan is not submitted to the court within four months (two months in some cases) of the date on which the debtor entered into external administration, the court may commence bankruptcy proceedings.

If the administrator fails to perform the reorganisation plan, the creditors can request that the court terminate the authority of the existing administrator and appoint a new administrator.

The court may start bankruptcy proceedings at the end of the external administration if it does not approve the report of the external administrator, and one month after the end of the external administration if the external administrator fails to submit its report to the court.

#### Insolvency processes

##### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

Creditors must be notified of creditors' meetings and of all major bankruptcy issues. The official sources for the publication of information on bankruptcies are the unified federal register of bankruptcies (available on the internet) and the *Kommersant* newspaper.

During bankruptcy proceedings, creditors are generally represented by a creditors' meeting. Shareholders or participants of the debtor can also be represented in creditors' meetings but do not have any voting rights. The shareholders' representatives can appeal to court against decisions made by insolvency office holders and resolutions of creditors' meetings. The creditors may also form a creditors' committee (see question 29).

The creditors meeting is convened by an insolvency office holder, the creditors' committee, creditors or authorities whose claims amount to 10 per cent or more of the total creditors' claims or one-third of the total number of creditors or authorities. The agenda of the creditors' meeting shall be provided in the request for convening the meeting. The insolvency office holder is not authorised to amend the agenda proposed by the creditors or the authorities. The creditors' meeting shall be held within three weeks (or earlier if so specified in the request) after receipt of the request of the creditors or authorities. The creditors' meeting shall take place at the location of the debtor or its management bodies.

According to the Rules regarding the organisation of creditors' meetings and meetings of the creditors' committees approved by the

Russian Government Order dated 6 February 2004, the insolvency office holder shall provide the creditors' meeting with documents regarding the debtor's financial condition, the status of bankruptcy procedures and other documents that are required to decide the issue of the creditors' meeting agenda and, therefore, the creditors are entitled to request such documents to be provided by the insolvency office holder.

The main reporting duties of an insolvency office holder provided by the Bankruptcy Law include the following:

- at the supervision stage: a supervisor will provide the court with a report regarding his activity and minutes of the first creditors' meeting with the opinion on the debtor's financial condition and justification of the possibility or impossibility of the financial rehabilitation of the debtor;
- at the stage of financial restoration: an administrative manager will provide the creditors' meeting with an opinion regarding the extent to which the payment schedule has been followed and a plan of financial restoration based on the debtor's report;
- at the stage of external administration: an external administrator will provide the creditors' meeting with the report of the external administration results; and
- at the stage of the bankruptcy proceedings: a bankruptcy trustee will provide the creditors' meeting with a report on his activity and information on the debtor's financial condition and assets, etc.

Decisions made at creditors' meetings as a rule require a simple majority of votes of the creditors present.

Generally, the Bankruptcy Law does not provide for any rules in relation to pursuing the estate's remedies by creditors against third parties, but the right to bring proceedings against third parties is confined to the insolvency office holders. Creditors may, however, ask the court to suspend legal proceedings against the debtor. They are also entitled to bring a limited number of actions outside bankruptcy proceedings. Creditors whose claims were not fully satisfied in the course of the liquidation will have the right to claim against third parties that unduly received the debtor's property.

Given that it is likely that any release of liabilities owed to the debtor by third parties may breach the rights and interests of the debtor's creditors as a whole and that the Bankruptcy Law sets out that transactions entered into in the course of the bankruptcy procedure with a purpose to breach the rights and interests of the debtor's creditors are voidable, such a release is not considered possible.

#### Enforcement of estate's rights

##### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Russian law does not provide any procedure by which the creditors can pursue the estate's remedies if the insolvency administrator has no assets to pursue a claim.

#### Creditor representation

##### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

According to the Bankruptcy Law, if the company has 50 or more creditors, then a creditors' committee must be formed. The creditors' committee may consist of three to 11 members. If there are fewer than 50 creditors, the formation of a creditors' committee is optional. The members of the creditors' committee are elected at the creditors' meeting for the period of supervision, financial restoration, external administration and bankruptcy proceedings. Only individuals nominated by the creditors (or state authorities) may be elected as members of a creditors' committee. The creditors' meeting can terminate the powers of the creditors' committee at any time.

The creditors' committee represents the interests of creditors, controls the insolvency office holder and fulfils other duties provided to it by the creditors' meeting. The creditors' committee is entitled to request information from the insolvency office holder, challenge his or her actions and take other decisions within the powers conferred on the creditors' committee by the creditors' meeting.

The creditors' meeting and creditors' committee allow creditors to influence the bankruptcy procedure. The exclusive competence of the creditors' meeting includes issues such as whether to:

- proceed with financial restoration, external administration or liquidation or enter into a composition; and
- approve the reorganisation plan, the financial restoration plan and the payment schedule, etc.

The Bankruptcy Law does not specifically regulate the procedure of convening and holding the meeting of the creditors' committee. This is a matter for the rules of the creditors' committee approved by the committee. The creditors' committee may decide that the insolvency office holder is in charge of notifying the members of the creditors' committee about the meeting and other connected organisational matters. Decisions made by the creditors' committee require a simple majority of votes when a vote is taken by all members of the creditors' committee. The creditors' committee may elect a representative to perform its duties.

According to the Bankruptcy Law, the insolvency office holders are entitled to retain advisers (other entities) to facilitate performance of their duties, the creditors' meeting may also take a decision on that issue. Costs for the services of advisers retained by the insolvency office holders are compensated by the debtor within the limits provided by the Bankruptcy Law. However, if a decision on retaining of advisers was taken by the creditors' meeting, the general rule is that the creditors who voted for such decision must pay for the services of such advisers pro rata to the amount of their respective claims included in the register of creditors' claims as of the date of the meeting.

#### Insolvency of corporate groups

##### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Russian law does not establish any insolvency proceedings for corporate groups. Therefore, insolvency proceedings initiated regarding a parent company and its subsidiary cannot be combined for administrative purposes. Furthermore, the assets and liabilities of the parent company and its subsidiary cannot be combined into one pool for distribution purposes.

Since Russian bankruptcy law does not regulate cross-border cooperation between domestic and foreign administrators, it is not possible to transfer assets from an administrative procedure in Russia to another country.

#### Appeals

##### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Court orders passed in insolvency proceedings can be appealed without any specific permission.

Court rulings passed as a result of adjudication by the court of motions, applications and complaints, as well as rulings that establish the amount of the creditor's claim can be appealed to the appellate court within 10 days from the date they were passed. Upon consideration of the appeal, the appellate court either upholds or reverses the ruling.

A further appeal can be filed with the court of cassation within two months from the date of the resolution of the appellate court. Upon consideration of the cassation appeal, the court renders a resolution upholding, amending/reversing the order or the resolution of the court of appeal or returning the case to an inferior court for reconsideration.

Subsequent appeals may be filed with the Collegium of the Supreme Court of Russia in charge of considering commercial disputes. The Collegium only accepts the cases for consideration on exceptional basis, namely, if there were severe violations of material or procedural law. Upon review of the cassation appeal, the Collegium issues a resolution upholding, amending or reversing the judicial acts of the inferior courts or returning the case to the inferior court for reconsideration.

The Collegium's resolutions could be finally referred to the Presidium of the Supreme Court within three months of the date of the resolution for a supervision review.

Other court orders that are envisaged by the Law on Insolvency but are not envisaged by the Arbitrazh Procedure Code (eg, a ruling on acceptance of an application for declaration of insolvency) can be appealed to the appellate courts within 14 days of the date they were passed. These orders can be further appealed only to the Presidium of the Supreme Court within three months of the date of the ruling they were passed.

Russian law does not provide requirement of post security to proceed with an appeal.

## Claims

### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Unpaid creditors are allowed to submit their claims at any time during the bankruptcy proceedings. The claims are recorded in the register of creditors' claims, which can be held either by an insolvency office holder, or, subject to a resolution of the creditors' meeting, by a professional securities market participant. The register is maintained in roubles; therefore, all foreign currency claims must be converted into roubles at the Russian Central Bank exchange rate in effect on the date of the start of the relevant bankruptcy stage. These sums will represent the amount of creditors' claims against the debtor.

To participate in the first creditors' meeting (see question 10), the creditors must submit the claims to the debtor, the court and the supervisor within 30 days of the date of publication of the start of the supervision stage (see question 10).

Creditors who fail to file their claims during the supervision stage may submit their claims during financial restoration or external administration. Claims may also be submitted within two months of publication that the debtor had commenced bankruptcy proceedings.

Generally, creditors' claims not submitted within this time period are satisfied out of any assets that remain after the claims submitted within this period are satisfied.

The Bankruptcy Law does not regulate the transfer of claims by creditors during a bankruptcy procedure. Therefore, the terms of a transfer regulating the relations between transferor and transferee, such as acquisition discount, do not affect the amount payable by the debtor. Once the claims are transferred from one creditor to another, the respective changes shall be made to the register of the creditors' claims, otherwise the claims of the new creditor could not be satisfied and it could not participate in the creditors' meeting. Under the Bankruptcy Law, the claims of creditors can be included or excluded from the register of the creditors' claims only on the basis of a court decision. Thus, after the claims are transferred, the new creditor must procure a court's decision on procedural legal succession. In practice the new creditor can have difficulties in obtaining such court decision.

The claims for contingent or unliquidated amounts are not included in the register of the creditors' claims as such.

## Modifying creditors' rights

### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

In accordance with Russian law, courts cannot change the rank of a creditor's claim as this is established by law (see question 33).

## Priority claims

### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

During bankruptcy proceedings, legal costs, insolvency office holders' fees, operating costs and company expenses, as well as debts arising during the bankruptcy proceedings, rank ahead of all other claims.

Other claims (as provided under the Bankruptcy Law) are categorised as follows:

- personal injury claims (highest ranked claims);
- employees and copyright claims (second highest ranked claims); and
- all other claims (including claims arising out of the compulsory payment and claims by secured creditors) (third highest ranked claims).

Generally, claims by secured creditors will rank first among the 'other claims' referred to above. These are paid from the company's pledged or mortgaged assets before other claims are paid. Under the Bankruptcy Law the pledgee or mortgagee is entitled to receive up to 70 or 80 per cent (but not more than the total indebtedness under the secured obligation) from the proceeds of sale of the pledged or mortgaged assets. Out of the balance 15 to 20 per cent of the proceeds are used to satisfy first and second-ranking claims and 5 to 10 per cent to repay the court expenses and fees of bankruptcy managers, etc.

Certain specifics exist in relation to ranking of claims of creditors of credit organisations, private pension funds and developers.

## Employment-related liabilities in restructurings

### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

According to the Employment Code of the Russian Federation (the Employment Code), the general rule is that reorganisation does not constitute a ground for termination of employment relations. However, the employees on their own initiative may refuse to continue working for the company after its reorganisation. In such cases, employment contracts with those employees shall be terminated as prescribed by Russian employment legislation. The employees are not entitled to any special severance payments unless otherwise provided for in their employment contracts or a collective bargaining agreement.

If the assets of a company are transferred to a new business owner, the latter is entitled to terminate the employment of the chairman of the company, their deputies and the chief accountant. If the employment contracts with these employees are terminated by the new business owner, the employees are entitled to a severance payment in the amount of not less than three months' average salaries. However, based on the existing court practice, this ground for termination of employment only applies in a limited number of cases where the assets of the company are transferred from public ownership to private ownership and vice versa (eg, upon privatisation or nationalisation of a company) and does not apply in general asset deals. In particular, a change in shareholders, generally, does not constitute a ground for terminating employment of the company's chairman, his or her deputies and the chief accountant.

If redundancy is a part of the company's restructuring, the company must notify its employees and any trade unions on termination of their employment at least two months (or three months in the event of mass dismissals) before such termination. The company must also notify the local employment service of the forthcoming redundancies within the same time periods. The company must also offer employees whose positions are to be made redundant vacant positions in the company that are suitable for the employees based on their qualifications and health, including less-qualified and lower-paid positions, if any exist. Should the employee refuse the proposed available vacant positions or should the company have no available vacant positions in the same territory where the employee is located, the employee's employment may generally be terminated with payment of a statutory severance payment.

Some categories of employee have preferential rights to employment and should be made redundant last. First of all, employees employed in the same position with a higher performance rate and qualification should be made redundant after colleagues with a lower performance rate. If the performance rate and qualification are equal, certain criteria provided by law must apply to determine preferential rights to employment (eg, married individuals with two or more dependents, employees who are the only working individual in their family, employees improving their qualifications on the initiative of the employer have preferential rights to employment).

Some categories of employees are protected against dismissal at the employer's initiative, including dismissal because of redundancy

(eg, pregnant women, women with children under three years of age and some other categories of employees).

In addition to general payments upon termination of employment employees dismissed because of redundancy are entitled to one month's average salary as severance pay. An employee may also be entitled to his or her average salary for the second and third months after termination of employment in exceptional circumstances provided that he or she has not found new employment.

Under Russian law, voluntary or involuntary liquidation of a solvent company constitutes a stand-alone ground for employment termination. Employees dismissed because of liquidation of a company are entitled to the same payments as described above for redundancy. According to Russian law, in liquidation proceedings such employees' claims rank second, after personal injury claims.

As to the procedure for termination of employment, the Employment Code provides that the employer, which is or plans to be liquidated, must notify each of its employees no later than two months before the termination of their employment in connection with the liquidation. The employer shall also notify the local employment service of the forthcoming dismissal of the employees two months (or three months in the event of mass dismissals) before such employment termination.

According to the Bankruptcy Law, employees are represented in the bankruptcy proceedings by a person elected by them. The procedure to be followed in terminating employment and the amounts payable to employees are the same as described in relation to liquidation.

### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Under Russian law, employers pay social insurance contributions to the Pension Fund of the Russian Federation, Social Insurance Fund of the Russian Federation and Federal Compulsory Medical Insurance Fund with respect to all employees. In accordance with Bankruptcy Law, claims against employers in respect of social insurance contributions that have arisen after bankruptcy proceedings were initiated are included in the category of current payment that ranks ahead of all other claims (see question 31). Claims to pay social insurance contributions that should have been paid before bankruptcy proceedings were initiated are ranked third in the insolvency proceedings. These claims are asserted by authorised government bodies. No special remedies are set out in the Bankruptcy Law with respect to these claims.

In practice, companies in Russia may also choose to enter into pension agreements with private pension funds to establish corporate programmes for the benefit of their employees (in addition to payments to the Pension Fund of the Russian Federation). Employees have no claim for unpaid contributions under the said corporate programmes against the employer unless otherwise specifically agreed between the employer and the employees.

### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The management of the debtor, the relevant bankruptcy manager or the respective officers of the debtor are generally in charge of compliance by the debtor with environmental laws. The debtor (as well as the relevant officers) could be subject to criminal, civil or administrative liability should the debtor breach any environmental laws. Russian law provides that any damage caused to the environment should be compensated for. According to the Bankruptcy Law, in cases where termination of the debtor's business could cause technogenic or ecological catastrophes, or both, or the death of humans, the costs of taking measures to prevent such consequences are payable ahead of other claims. Apart from this, Russian law does not provide any special regime for compliance with environmental laws in the course of the bankruptcy procedures.

### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

In accordance with Russian law, in the event of a debtor's reorganisation, its liabilities are transferred to its legal successors. The situation is different where a debtor was recognised as insolvent and is subject to involuntary liquidation. On involuntary liquidation of a legal entity responsible for damage to life and health, the corresponding payments shall be capitalised for payment to the injured party, in accordance with the rules established by Russian law. Once the capitalised payments are transferred to the relevant off-budgetary funds, they then effect the payments to the injured parties.

### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Distributions to creditors may be made at any stage of the bankruptcy proceedings. Each tier of creditors must be satisfied in full before the next tier can receive any payment. Claims not satisfied because of the insufficiency of the debtor's assets are deemed cancelled.

If the amount received by the company for its business and assets is lower than the total amount of creditors' claims, then the proceeds can be distributed pursuant to a composition agreed upon by the creditors (see question 12).

### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

Russian law does not provide for any specific grounds to annul or set aside any transactions in the course of voluntary or involuntary liquidation of a solvent company or its reorganisation. However, if a company is undergoing reorganisation, creditors are entitled to request early performance of the debtor's obligations or, if such performance is impossible and the creditor was not provided with the adequate security, termination of the relevant obligations and compensation for losses in connection with such termination.

As to the bankruptcy procedures the following transactions can be invalidated by court (as well as the transactions that can be invalidated according to general grounds set out in the Civil Code):

- transactions entered into by the debtor within a year before or after filing of the bankruptcy petition if inadequate consideration was provided by the other party to the debtor under such transaction (eg, sale by the debtor of assets at a price that is materially less than the market value of such assets);
- transactions made by the debtor within three years before or after filing of the bankruptcy petition with the purpose to circumvent the economic interests of creditors provided the relevant counterparty knew about such purpose (eg, transfer of property by the debtor without compensation, in such a case the knowledge of the counterparty is assumed); and
- transactions entered into by the debtor within a month (in some cases six months) before or after filing of the bankruptcy petition and resulting in the preferential satisfaction of the claims of one creditor over others (eg, a transaction that leads or could lead to a change in creditors' rankings).

Claims for invalidation of these transactions can be brought by the insolvency office holder, on their own initiative or pursuant to a decision of the creditors' meeting or creditors' committee, or by the creditor or a competent authority in cases where the amount of indebtedness owed to such creditor or the authority comprises 10 per cent of the total amount of claims included on the register of creditors' claims.

The limitation period for challenging all of the above transactions is one year from the date on which the relevant claimant became aware of or should have become aware of the grounds for invalidating the transaction.

An insolvency office holder may also apply to the court at any stage of bankruptcy procedure for invalidation of any transactions concluded by the company provided that such transactions were made in violation of the bankruptcy law (eg, without relevant consent).

Invalidation of a transaction generally leads to bilateral restitution, meaning that each party returns everything received under the transaction to the other party.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

See question 39.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

##### Civil liability

According to the Bankruptcy Law, if a debtor is declared insolvent as a result of actions (or omissions) of the debtor-controlling persons, such persons shall be liable for the debtor's obligations if the debtor's assets are insufficient. Such liability is subsidiary. Debtor-controlling persons include persons who have or had, within less than three years before filing of the bankruptcy petition, the right to give binding instructions to the debtor or who could otherwise determine the actions of the debtor.

Unless proved otherwise, it is assumed that the debtor-controlling persons caused the debtor's insolvency if:

- actions or omissions, to their benefit or approved by them, caused damage to creditors' property interests (including voidable transactions as indicated in question 39);
- any accounting or other company documents that, according to Russian law, must be kept by the company, are lost or such documents contain misleading or incomplete information as a result of which the bankruptcy procedures became significantly more difficult (in this case, the person responsible for maintaining such documents will have subsidiary liability with respect to the company's debts); and
- the amount of third ranking creditors' claims (the principal indebtedness) arisen as a result of violation of tax law by the debtor or its chief executive officer or officers exceeds 50 per cent of the total amount of third-ranking creditors' claims (the principal indebtedness) as of the date of closing of the creditors' claim register (in this case, the debtor's chief executive officer or officers at the time of violation of tax law will have subsidiary liability with respect to the company's debts).

In case of breach of the obligation to file the bankruptcy petition as provided for by the Bankruptcy Law, the CEO of the debtor can be liable for the debtor's obligations starting from the date when the term for filing of such petition has expired. Such liability is also subsidiary.

In the event of breach of the Bankruptcy Law by shareholders and management of the debtor, they can be held liable for losses caused by such breach.

Additionally, the Civil Code provides that the management of a company as well as any person de facto controlling it shall act in the interests of the company, reasonably and in good faith. Breach of this duty can result in the liability of said persons to damages for losses caused by such breach.

##### Criminal liability

The company's management and its shareholders may be criminally liable under the Criminal Code of the Russian Federation of 13 June 1996 for:

- misbehaviour in the course of bankruptcy (concealment of assets, illegal satisfaction of creditors' claims etc);
- fictitious bankruptcy (where a company initiates bankruptcy proceedings at a time when it is in fact able to fully settle creditors' claims); and
- intentional bankruptcy (where there was an intention to cause the bankruptcy and not to act in the company's interests but in the furtherance of personal or third parties' interests).

### Update and trends

From 1 October 2015 the insolvency of natural persons became possible in Russia. The bankruptcy procedures applicable to natural persons include debt restructuring, sale of assets and composition. The first year of application of this new legislation revealed some issues with insolvencies of natural persons, such as bad-faith debtors, possible high cost of procedures, unclear procedures for spouses as joint debtors and others. Recently, Russian courts started to apply bankruptcy law to foreign citizens, but the court practice has not been formed yet, and it is not consistent so far.

The discussion topics devoted to the development of the insolvency laws include cross-border insolvencies, improvement of restructuring and bankruptcy proceedings. Although according to the discussions, some draft laws are being prepared, and it is difficult to predict whether any amendments to bankruptcy laws should be expected in the near future.

The management of the debtor may also be liable for providing misleading information in the financial or accounting statements (documents), or both, of a financial organisation (bank, insurance company, etc) if the management's intention was to suppress the fact that the organisation meets the insolvency criteria.

##### Administrative liability

The primary distinctions between administrative and criminal liability are that the former attaches more easily than the latter and the potential sanctions are less extreme. Offences under the Russian Code on Administrative Offences include misbehaviour in the course of bankruptcy and intentionally or fictitiously causing the company's insolvency. The administrative liability will be attached to the shareholders, management and the company itself.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

According to Russian law, a parent corporation can be responsible for the liabilities of its subsidiary if such parent corporation is entitled to determine decisions of the subsidiary.

The parent corporation and subsidiary are jointly and severally liable for the transactions entered into by the subsidiary in performance of the parent corporation's instructions or with its consent.

In the case of insolvency of the subsidiary because of the fault of the parent corporation the latter has a subsidiary liability in relation to the debts of the subsidiary.

The parent corporation can also be regarded as a debtor controlling person or a person de facto controlling the subsidiary (see question 41 in relation to liability of such persons).

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There are no restrictions on claims by insiders or non-arm's length creditors against their corporations in bankruptcy proceedings taken by those corporations; however, the Bankruptcy Law sets out certain grounds for invalidation of non-arm's length transactions of insolvent companies (see question 39).

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Generally, once the debtor is placed under supervision (see question 10) no execution can be levied on the pledged assets of the debtor, including on an out-of-court basis. At further stages of the insolvency case, the court could permit a secured creditor in certain circumstances to levy execution over the pledged assets of the debtor.

**Corporate procedures****45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

A company that is solvent can be liquidated pursuant to a decision of its shareholders or participants and is subject to their control. The decision to liquidate the company must be made by a qualified majority of the shareholders attending the vote (subject to a quorum of more than 50 per cent) for a joint-stock company or by unanimous consent of all participants for a limited liability company. Corporate liquidation may only be implemented if the company has sufficient assets to satisfy all creditors' claims, otherwise a bankruptcy petition must be filed to initiate bankruptcy proceedings.

To liquidate the company, a liquidation commission (liquidator) is appointed by the company's shareholders or participants. The liquidator has rights to manage the company and, in particular, to deal with its assets to satisfy creditors' claims. The liquidator must publish information on the company's liquidation specifying the period within which the creditors may submit their claims. Such a period cannot be less than two months after publication.

If the liquidator finds that the company's assets are insufficient to satisfy all creditors' claims, he or she must file a bankruptcy petition with the court. In this case, the company will undergo only the liquidation stage of bankruptcy proceedings. The liquidator must publish information on the company's bankruptcy and its liquidation. Creditors may submit their claims within one month of publication. This renders the company subject to the general bankruptcy proceedings described in questions 10 and 12.

**Conclusion of case****46 How are liquidation and reorganisation cases formally concluded?**

Liquidation under the Bankruptcy Law is concluded by a court passing a relevant resolution after the final distribution of proceeds from the realisation of the debtor's assets is made or by approving a composition. Corporate liquidations are concluded with the distribution among the company's shareholders or participants of the assets remaining after creditors' claims are satisfied. Formally, bankruptcy proceedings end when a winding-up entry is made in respect of the company in the state register of legal entities.

The conclusion of financial restoration and external administration is generally subject to restoration of the company's solvency or its entering into a composition. If the financial restoration is not successful, external administration or bankruptcy will be commenced.

If the external administration is not successful, bankruptcy will be commenced. Provided the financial restoration or the external administration is successful then the bankruptcy proceedings will terminate and a relevant court resolution will be passed.

**International cases****47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Foreign judgments could be enforced in Russia based on international treaties.

Russia is not a signatory to any specific international bankruptcy treaty. The Bankruptcy Law also provides that in the absence of such an international treaty foreign judgments on insolvency proceedings shall be recognised in Russia on the principle of reciprocity.

Foreign creditors have the same status as Russians, but foreign debtors are not subject to Russian bankruptcy proceedings. Foreign-owned assets located in Russia should not be subject to Russian bankruptcy proceedings.

The UNCITRAL Model Law on Cross-Border Insolvency is not being considered for incorporation into Russian law.

**COMI****48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

Russia is not a member state of the European Union and the EU Regulation on Insolvency Proceedings does not apply. Russia has also not enacted the UNCITRAL Model Law on Cross-Border Insolvency. As such, the concept of COMI has no application in Russia.

**Cross-border cooperation****49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

As stated in question 47, the foreign court decisions on insolvency (bankruptcy) are recognised in Russia based on the principle of reciprocity or international treaties.

Apart from the above, Russian bankruptcy legislation does not provide any specific rules in respect of cross-border cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings.



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In Russia there is no procedure for recognition of foreign proceedings and only foreign final judgments on the merits can be recognised (thus, for instance, no act of a foreign court on interim relief can be recognised as such act is not a final court judgment on the merits). Applications for recognition and enforcement of foreign monetary judgments (or arbitral awards) can be filed only in bankruptcy proceedings. If the proceedings on recognition and enforcement were commenced before initiation of insolvency proceedings then the creditor may either continue them or terminate them and file an application in insolvency proceedings.

There were some attempts in Russia to recognise foreign proceedings or to cooperate with foreign courts but they failed because of lack of legislation, as stated above.

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**Cross-border insolvency protocols and joint court hearings**

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

No cross-border insolvency protocols are currently in place in Russia, nor have any other arrangements been entered into by the Russian courts to coordinate proceedings with courts in other countries. No communication or joint hearings have taken place in cross-border cases between the Russian courts and those of other countries.

# Singapore

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The answers set out below are with reference to companies only, and do not cover any other entities unless expressly stated otherwise. The term 'bankruptcy' in Singapore law refers only to the insolvency of individuals, but any references to 'bankruptcy' in this chapter refer to the liquidation and winding up of companies.

The liquidation and winding up of companies is governed by the Companies Act (the Act) and its related subsidiary legislation, as are schemes of arrangements and judicial management (ie, reorganisations).

Under the Act, the most common ground to wind up a company on the grounds of insolvency is that the company is unable to pay its debts (section 254(1)(e) of the Act). Under section 254(2) of the Act, a company is deemed to be unable to pay its debts if:

- a demand for a sum exceeding S\$10,000 due to a creditor has been duly served on the company requiring the company to pay the sum so due and the company has for three weeks thereafter neglected to pay the sum or to secure or compound for it to the reasonable satisfaction of the creditor;
- execution or other process issued on a judgment, decree or order of any court in favour of a creditor of the company is returned unsatisfied in whole or in part; or
- it is proved to the satisfaction of the court that the company is unable to pay its debts as they fall due; and in determining whether a company is unable to pay its debts the court shall take into account the contingent and prospective liabilities of the company.

A company is not insolvent at law merely because its current liabilities exceed its current assets. Rather, a creditor either has to show that the company has failed to meet a current demand for a debt already due, or whether, on balancing the overall liabilities against the assets of the company, there was a deficit. Under the latter question, such overall liabilities would include present, future and contingent creditors of the company, and the assets to be valued include all assets of the company, and not just current assets.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Applications for the liquidation or reorganisation of a Singapore company come under the sole purview of the Singapore High Court. Singapore does not have specialised insolvency courts dealing exclusively with insolvency matters, although most insolvency matters now appear to be fixed before judges who have expertise in this area. There are no limitations on the High Court's jurisdiction or power to deal with matters pertaining to corporate insolvency.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

While the winding-up regime under the Act applies to all of the following companies, additional requirements as to their winding up are imposed under their industry-specific legislation: electricity licensees (Electricity Act), companies carrying on insurance or insurance broking business (Insurance Act), trust companies (Trust Companies Act) and designated clearing houses (Securities and Futures Act).

The insolvency of individuals (Bankruptcy Act), limited liability partnerships (Limited Liability Partnerships Act) and registered business trusts (Business Trusts Act) are dealt with under their respective legislation and its related subsidiary legislation.

Assets of the company that have securities (mortgages, charges, pledges among others) against them would generally be excluded from the claims of creditors, unless the security holders choose to forfeit their security over the relevant assets, in which case the assets so forfeited would return to the general pool of the company's assets (see questions 6 and 7).

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There is no specific legislation that regulates the insolvency of a government-owned enterprise (ie, a company that is partially or wholly owned by the state or state-owned companies), and generally procedures and creditors' remedies that are applicable to all companies incorporated under the Act will apply to insolvent government-owned enterprises. There are public interest exceptions to various insolvency regimes that may apply (although not exclusively) to government-owned enterprises. A court may exercise its discretion not to wind up an insolvent company on public interest grounds, or may grant an order to place a company under judicial management even where the statutory purposes (see question 12) are not met.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

While there is specific legislation that regulates the insolvency of specific institutions with a 'public interest' element, such as insurance or insurance broking companies (the Insurance Act), securities exchanges or securities market (the Securities and Futures Act), electricity licensees (the Electricity Act) and railway licensees (the Rapid Transit Systems Act), Singapore has not enacted legislation to deal with financial difficulties of institutions solely on the grounds that such institutions are 'too big to fail'.

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**Secured lending and credit (immoveables)**


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**6 What principal types of security are taken on immoveable (real) property?**

The principal types of security taken on immoveable (real) property are legal mortgages and equitable mortgages.

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**Secured lending and credit (moveables)**


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**7 What principal types of security are taken on moveable (personal) property?**

The most common form of security taken on moveable property is a charge, either fixed or floating. Pledges, liens and retentions of title are less common and less popular.

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**Unsecured credit**


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**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

If an unsecured creditor has obtained a final judgment from the courts in its favour but is still unable to obtain payment from the debtor, it may seek to enforce judgment for the payment of a debt in the following ways:

- issuing a writ of seizure and sale over moveable or immoveable property;
- applying to garnish any debt due or accruing to the debtor from some third party, including money in a bank account; or
- applying for the appointment of a receiver by way of equitable execution.

Such applications, if not heavily contested, will usually take about 21 days from the date of the filing of the writ.

The creditor may also seek to wind up the debtor. The process of applying for a winding up usually takes about 21 days to about 35 days from the date of the application to wind up to the date a winding-up order is obtained. Subsequently, the liquidation and distribution of the company's assets by the liquidator may take from six months to two years, but the length of time taken will ultimately depend on the complexity of the company's operations and whether there are any disputes.

There are no provisions dealing with 'pre-judgment attachments' as such but where court proceedings have been commenced, a creditor may apply for an injunction to freeze the debtor's assets if it can show that there is a risk that it will dissipate them and thereby frustrate any judgment obtained against it.

Where a foreign creditor seeks to bring proceedings against a debtor in Singapore, no special procedures apply except that it may be required to provide security for the debtor's legal costs (in the event costs are awarded against that foreign creditor). Where a foreign creditor has already obtained a foreign judgment against the Singaporean debtor, it may register the judgment with the Singapore courts and, once registered, the judgment may be enforced as if it were a local judgment. This procedure is only available if the foreign judgment is one that falls under the Reciprocal Enforcement of Foreign Judgments Act or the Reciprocal Enforcement of Commonwealth Judgments Act. If the judgment is one that falls outside these two acts, the foreign creditor will need to commence proceedings to sue on the foreign judgment as a debt.

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**Voluntary liquidations**


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**9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?**

A debtor's voluntary winding up may be commenced by its members. To commence a members' voluntary liquidation, the company's board of directors must make a statutory declaration that they have inquired into the affairs of the company and are of the opinion that the company will be able to pay its debts in full within a period not exceeding 12 months after the commencement of the winding up. The members should then pass a special resolution to voluntarily wind up the company. They will have to pass an ordinary resolution to appoint a liquidator for the purposes of winding up the affairs and distributing the assets of the company.

If no statutory declaration of solvency is made by the directors, the liquidation will proceed as a creditors' voluntary winding up. In addition to the special resolution of the members to voluntarily wind up the company, the company must also convene a meeting of its creditors to consider the proposal for a voluntary winding up. The company will appoint a liquidator, subject to any preference the creditors may have as to the choice of liquidator.

The company must cease to carry on its business. The corporate state and powers of the company will, notwithstanding anything to the contrary in its articles of association, continue until it is dissolved. Any transfer of shares, not being a transfer made to or with the sanction of the liquidator, and any alteration in the status of the members made after the commencement of the winding up, will be void.

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**Involuntary liquidations**


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**10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

To involuntarily wind up a company, a creditor must apply to court. For the court to grant its application, it must establish that the company is unable to pay its debts either on the basis of the cash-flow test (ie, the company is unable to pay its debts as they fall due) or the balance-sheet test (ie, its liabilities exceed its assets). The applicant may also show that the company has failed to pay a sum demanded (where the sum must exceed S\$10,000) within three weeks after the demand, or that execution or other process issued on a judgment, decree or order of any court in favour of a creditor of the company was returned unsatisfied in whole or in part.

If the court orders that the company be wound up, the winding up is deemed to have commenced at the time of presentation of the application. Once a winding-up order is made (or provisional liquidator appointed), there is an automatic stay of any action against the company, and no action or proceeding may proceed, or be commenced, except by leave of the court. Any disposition of the company's property or any share transfer made after the commencement of the winding up is void unless the court orders otherwise.

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**Voluntary reorganisations**


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**11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

The Act provides for two forms of formal financial reorganisation: a scheme of arrangement pursuant to section 210 of the Act or a judicial management under Part VIIIA of the Act. While only the company may apply for a scheme of arrangement, both the company and its creditors may apply for an order of judicial management. As the question refers to a debtor commencing a financial reorganisation, we look here only at the scheme of arrangement. Judicial management will be dealt with in question 12.

To propose a scheme of arrangement, the company must apply to court for an order summoning a meeting of the creditors of the company, the members of the company, the holders of units of shares or class of holders or units of shares of the company, or a class of such persons. If the court grants the order, the company must send out a notice summoning the meeting and the notice must contain a statement explaining the effect of the proposed compromise or arrangement. The proposal must be approved at the meeting by a majority in number representing three-quarters in value of each class of creditor or member present and voting at the meeting, unless the court orders otherwise. If the meeting approves the scheme, it must be approved by the court, which may grant its approval subject to such alterations or conditions as the court thinks just.

A scheme of arrangement that has been thus approved is binding on all creditors and members of the company.

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**Involuntary reorganisations**


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**12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

A company or its creditors may apply to court for an order that the company be placed under the judicial management of a person known as a judicial manager. The court may grant such an order if it is shown that the company is or will be unable to pay its debts but that there is a reasonable prospect of rehabilitating the company or of preserving all or

part of the business as a going concern, or that otherwise the interests of creditors would be better served than by resorting to a winding up.

If the court grants an order for judicial management, the business and property of the company will be managed by a judicial manager for a period of 180 days subject to any further extensions that the court may grant and the board of directors becomes *functus officio*. In addition, during the period of the judicial management:

- the company may not be wound up;
- no receiver and manager of the whole of the company's property may be appointed; and
- there will be a moratorium on legal proceedings against the company and any steps to enforce any security or quasi-security save with leave of court or the consent of the judicial manager.

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

There is no express duty on a company to commence insolvency proceedings at any particular time. However, various rules apply to the directors of a company that has become insolvent and directors may choose to commence insolvency proceedings in order to avoid the effects of these rules:

- A director or other officer of a company may be criminally liable if he or she is knowingly a party to the contracting of a debt when he or she had no reasonable or probable ground of expectation at the time of the company being able to pay the debt. He or she may also be declared personally liable without limitation of liability for the payment of the whole or any part of the debt.
- A director's fiduciary duty to act in the company's best interest will, when the company is insolvent or near insolvent, also include taking into account the interests of its creditors. While creditors may not sue the director for a breach of this duty, the company (acting through its liquidators) may do so.

A company is generally not precluded from carrying on business while insolvent. However, the liquidator of the company has the power to recover property of the company which has been improperly dissipated while the company was insolvent, by avoiding the transaction as either an unfair preference or a transaction at an undervalue (see question 39).

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

Where a company is not currently insolvent but is reorganising under a scheme of arrangement, there is no legal prohibition against the company continuing to carry on business. Its ability to carry on business will depend on the terms of any agreement with its creditors. Any conditions applicable to the use or sale of the assets of the business or whether any special treatment is given to creditors who supply goods or services after the filing is determined by the terms of any agreement between the company and its creditors. Creditors who supply goods or services to allow the company to carry on business during the scheme of arrangement are usually provided special treatment for such debts to be paid for in preference to other creditors in order for the company to continue its business. While there is often a scheme manager administering the scheme of arrangement, the powers of the company's directors remain intact and unaffected.

Where the company is under judicial management, the judicial manager will take over the management of the company from its board of directors, and he or she is empowered to do all such things as may be necessary for the management of the affairs, business and property of the company. In addition, company property that is subject to a security or quasi-security may be sold as if it were unencumbered if the judicial

manager obtains the authorisation of the court and provided that the proceeds are used toward discharging the secured debt.

The company's creditors must be given a statement of the judicial manager's proposals for achieving the survival of the company as a going concern (or achieving any other purpose for which he has been appointed). Such proposals would include the use or sale of the assets of the business or whether any special treatment is given to creditors who supply goods or services during the period of judicial management. They vote on whether to accept those proposals, with or without modification. Once approved, the judicial manager must manage the company's affairs, business, and property in accordance with the proposals. The creditors may establish a committee to monitor the judicial manager's progress. Any revisions require the approval of a majority of the creditors. A creditor may also seek relief from the court on the ground that the company's affairs, business or property is being managed by the judicial manager in a manner that is unfairly prejudicial to the interests of the creditors or members. The court has wide powers to grant relief if such a situation is established.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings and the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

After a winding-up application is presented, there is no automatic stay of legal proceedings against the company. Instead, the court has discretion to make an order staying or restraining further proceedings in the action or proceedings on the application of the company, a creditor or a contributory. Once a winding-up order is made or a provisional liquidator appointed, there is an automatic stay of proceedings against the company unless the court gives leave for the proceedings to continue. Such leave will be granted if the court considers that, on the balance of convenience and the demands of justice, it is necessary that the action be continued. Conversely, leave will not be granted if it can be shown that the claim is one that could just as easily be dealt with in the winding up.

Upon the filing of a judicial management application, no order to wind up the company can be made and no legal proceedings (including enforcement of security) may be commenced or continued against the company or its property except with leave of the court. This moratorium continues upon the granting of an order for judicial management, but upon the granting of the judicial management order, apart from the court granting leave for proceedings to commence or continue, the judicial manager also has the power to allow individual claims against the company to proceed. In deciding whether to grant leave, the court will balance the interests of the applicant against the interests of the other creditors in seeking to give effect to the objectives of judicial management and the purpose of the moratorium, having regard to all the circumstances of the case and the likelihood of adverse consequences to the interested parties.

There is no automatic moratorium on actions against the company while a scheme of arrangement is being proposed. However, an application may be made to court for an order that proceedings pending against the company be stayed. A court will consider whether there is a scheme with sufficient particulars to enable it to assess that it is feasible and merits due consideration by the creditors when it is eventually placed before them in detailed form. The court also has to be satisfied that there is or that there would be a bona fide application.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

A liquidator is expressly empowered under the Act to raise any money required for the expenses of the liquidation by giving security over the assets of the company. If unsecured loans have been taken out by the liquidator post-liquidation, the post-liquidation creditors are entitled to priority over the pre-liquidation creditors if the loan was necessary for the beneficial realisation of the company's undertaking.

A judicial manager is expressly empowered under the Act to borrow money and grant security in respect of such loans over the property of the company.

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**Set-off and netting**

- 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

In a winding up, contractual and equitable rights of set-off are displaced by statutory set-off provisions. Credits, debts or other dealings may be set off against each other only if they are mutual. Also excluded from any set-off are debts or liabilities that are not provable in bankruptcy or which arise by reason of an obligation incurred at a time when the creditor had notice that a winding-up application relating to the company was pending.

When a company is under judicial management, the moratorium on civil proceedings does not include self-help remedies such as contractual set-off (*Electro Magnetic (S) Ltd (under judicial management) v Development Bank of Singapore Ltd* [1994] 1 SLR 734).

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**Sale of assets**

- 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

The sale of specific assets of companies pursuant to schemes of arrangement or under judicial management or by the liquidator is treated no differently from the sale of assets in any other situation. As a general rule, liabilities do not pass with assets but the owner of a new asset may take it subject to any encumbrances as to title that may have affected the seller. Stalking horse arrangements and credit bidding are not common but, in theory, are accepted as being possible. Although there is no reported decision on whether the Singapore Court would accept a credit bid, the Court would probably look at certain factors which include, inter alia, whether the bidder is a secured creditor or an unsecured creditor, whether the bid is made for secured collateral only or includes other assets, and whether the sale of the assets is a part of a reorganisation plan or a stand-alone sale. A creditor who was assigned rights by way of a legal assignment of the rights of a secured creditor should in theory be allowed to place a credit bid as this was a right that was vested with the original secured creditor.

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**Intellectual property assets in insolvencies**

- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

Whether an IP licensor or owner may terminate a debtor's right to use intellectual property assets licensed to it while the debtor is subject to winding-up proceedings depends on the terms of the licence agreement entered into between the parties. Quite commonly, the insolvency of the licensee is an event of default under the licence agreement that entitles the licensor to terminate the licensee's rights to use the licensed assets. A liquidator has no better right than the insolvent licensee and would not ordinarily be entitled to terminate the insolvent licensee's agreement with a licensor or owner of intellectual property rights and continue to use these rights or assets for the benefit of the insolvent licensee unless this is contractually provided for in the licence agreement. However, it would be highly unlikely that the terms of a licence agreement would so provide.

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**Personal data in insolvencies**

- 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Protection of personal data in Singapore is regulated under the Personal Data Protection Act 2012 (the PDPA). Pursuant to the Fourth Schedule to the PDPA, an organisation may disclose personal data about an individual without the consent of the individual in the circumstances set out therein. Specifically, one of the circumstances is when personal data is disclosed to a party or a prospective party to a business asset transaction with the organisation (paragraph 1(p) of the Fourth Schedule to the PDPA). 'Business asset transaction' means the purchase, sale, lease, merger or amalgamation or any other acquisition, disposal or financing of an organisation or a portion of an organisation or of any of the business or assets of an organisation other than the personal data to be disclosed under paragraph 1(p).

The disclosure under paragraph 1(p) is subject to the following conditions:

- the personal data are about an employee, customer, director, officer or shareholder of the organisation;
- relate directly to the part of the organisation or its business assets with which the business asset transaction is concerned; and
- in the case of disclosure to a prospective party to a business asset transaction:
  - the personal data must be necessary for the prospective party to determine whether to proceed with the business asset transaction; and
  - the organisation and prospective party must have entered into an agreement that requires the prospective party to use or disclose the personal data solely for purposes related to the business asset transaction.

Finally, if the organisation enters into the business asset transaction, the employees, customers, directors, officers and shareholders whose personal data are disclosed shall be notified that the business asset transaction has taken place and that the personal data about them has been disclosed to the party.

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**Rejection and disclaimer of contracts in reorganisations**

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

The making of a judicial management order does not (unless contractually specified) affect the contracts to which the company is a party. The judicial manager does not have the liquidator's power to disclaim onerous contracts; nor does he have the receiver's powers to cause the company to breach its contracts. The judicial manager has the statutory power to adopt a contract, pursuant to which personal liability will be attached, subject to any disclaimer. For contracts not adopted by the judicial manager, the judicial manager may choose not to perform them, following which the other contracting party may claim for damages for non-performance of the contract by the company. This is subject, however, to any contracts that may be avoided as unfair preferences and transactions at an undervalue, as to which see question 39.

The judicial manager is personally liable for any contract entered into or adopted by him unless he disclaims the liability. However, as an agent of the company the judicial manager is entitled to be indemnified out of the assets of the company in respect of this liability.

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**Arbitration processes in insolvency cases**


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**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Our answer to question 15 as to moratoria applies equally to arbitration proceedings for contractual and other civil disputes. However, the insolvency proceedings themselves and claims arising from statutory insolvency provisions are non-arbitrable, especially when third-party creditors of the insolvent company would be affected (*Larsen Oil and Gas Pte Ltd v Petroprod Ltd* [2011] SGCA 21).

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**Successful reorganisations**


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**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

There are no mandatory features required of a scheme of arrangement under section 210 of the Act. The scheme must be approved by a majority in number representing three-quarters in value of the creditors or class of creditors or members or class of members present and voting at the meeting. Separate meetings for each class will need to be called, and the test for determining the constitution of classes is that a class should comprise those persons whose rights are not so dissimilar as to make it impossible for them to consult together with a view to their common interest.

A scheme may incorporate the involvement or participation of an outsider who is neither a member nor a creditor of the company, but its binding force in relation to that outsider is derived from the scheme as a contract, or some other contract between that outsider and the company, and not the order of court. The scheme may also incorporate an express term requiring creditors to release guarantors of the company's obligations, although such a provision would have to be enforced by the company, and not, it would seem, by the guarantors who are non-parties.

The above issues do not arise in a judicial management.

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**Expedited reorganisations**


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**24 Do procedures exist for expedited reorganisations?**

There are no formal procedures for expedited or 'pre-packaged' reorganisations in Singapore. However, the Court of Appeal in Singapore has noted that all matters relating to schemes of arrangement should be done on an expedited basis as time is of the essence in such matters (*The Royal Bank of Scotland NV and another v TT International Ltd* [2012] SGCA 9).

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**Unsuccessful reorganisations**


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**25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

A scheme of arrangement will be defeated if it fails to secure the requisite statutory majority of votes in its favour (as to which see question 23) or the sanction of the court (even if the requisite statutory majority of votes is obtained). In deciding whether to sanction the proposed scheme, the court will consider whether the statutory procedure has been complied with, whether the resolutions are passed by the requisite majority in value and in number at meetings duly convened, whether the classes of creditors are fairly represented by those who attended the meeting, whether the scheme is fair and reasonable, and whether the company's creditors have been provided with sufficient information in order for them to make an informed decision. Where the creditors have passed the necessary resolutions, the court will generally not interfere with their decision as the creditors would be in a better position to determine for themselves what is in their commercial interests. However, if the court is not satisfied as to the bona fides of the resolutions, it may decline to approve the scheme of arrangement.

The terms of the approved scheme will usually set out the consequences of any breach by the company of the provisions therein. For example, it may be stipulated that the failure by the company to make payment of an instalment to the creditors will result in the termination of the scheme. However, it is also possible to include a fixed 'cure period' in the scheme document conferring upon the company the right to remedy any default by it within the 'cure period' stipulated.

A judicial management order may be prematurely discharged if:

- the creditors decline to approve the judicial manager's proposals;
- the court so orders by reason of the judicial manager acting in a manner unfairly prejudicial to the creditors or members; or
- it appears on the application of the judicial manager that the purposes of the judicial management order cannot be discharged.

When the judicial management order is discharged, the judicial manager automatically vacates office.

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**Insolvency processes**


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**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

We approach this question with respect to a court-ordered winding up of a company. It should be noted that a company may also be voluntarily wound up by creditors when it is insolvent.

Once the court has ordered a company to be wound up, it will appoint a liquidator. Within 14 days of his or her appointment, the liquidator must lodge with the Registrar of Companies and with the official receiver a notice of his appointment and of the situation of his or her office.

Within 14 days from the date of the winding-up order, the directors and such other persons specified in the Act must submit to the liquidator a statement as to the affairs of the company as at the date of the winding-up order showing:

- the particulars of its assets, debts and liabilities;
- the names and addresses of its creditors;
- the securities held by them respectively;
- the dates when the securities were respectively given; and
- such further information as is prescribed or as the liquidator requires.

The liquidator must then as soon as practicable submit a preliminary report to the official receiver:

- as to the amount of capital issued, subscribed and paid up and the estimated amount of assets and liabilities;
- if the company has failed, as to the causes of the failure; and
- whether, in his or her opinion, further inquiry is desirable as to any matter relating to the promotion, formation or failure of the company or the conduct of the business thereof.

The liquidator may summon general meetings of the creditors or contributories for the purpose of ascertaining their wishes, and he must do so if so required by the creditors or contributories. Otherwise, he or she may exercise his or her own discretion in the management of the affairs and property of the company and the distribution of its assets.

The company's creditors and contributories may require the appointment of a committee of inspection to act with the liquidator, but no such committee need be appointed if not so required. Where no committee of inspection is appointed, the official receiver will act in its stead. For more on the committee of inspection, see question 28.

After a period of six months from the date of appointment, the liquidator must within one month lodge with the official receiver an account of his or her receipts and payments and a statement of the position in the winding up, and this must be done every six months thereafter. Upon such lodgement, the liquidator must notify every creditor and contributory that the account has been made up. The notification must be made when he or she next forwards any report, notice of meeting, notice of call or dividend. The notice must inform the creditors and contributories when and where the account may be inspected.

Creditors and contributories are also permitted to inspect the liquidator's minute books.

As a general rule, creditors may not bring proceedings against third parties in relation to losses suffered by the company. However, there are two exceptions where a creditor may apply to court rather than depending on the liquidator to do so: where the company has engaged in fraudulent trading, and where a promoter or an officer of the company has misapplied or retained or become liable or accountable for any money or property of the company or been guilty of any misfeasance or breach of trust or duty in relation to the company.

#### **Can a reorganisation plan provide for release of liabilities owed by third parties not part of the debtor group?**

A scheme of arrangement can release a debt owed by a third party where the scheme of arrangement expressly provides for such and if the requisite creditor approval has been obtained under the scheme.

#### **Enforcement of estate's rights**

##### **27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

A creditor may not bring legal proceedings against a third party for and on behalf of the company in liquidation. As a practical matter, however, a creditor may take an assignment of the claim from the company in which case the right to the fruits of the claim will belong to him or her (*Re Vanguard Energy Pte Ltd* [2015] SGHC 156).

#### **Creditor representation**

##### **28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

As noted in question 26, in a compulsory liquidation, the general body of creditors and contributories can compel the appointment, and decide the composition, of a committee of inspection, which will consist of members of this general body.

The committee of inspection plays a supervisory role in relation to the liquidator, who has a duty to have regard to their directions in administering the assets of the company. In addition, the liquidator must be authorised by the committee of inspection (or the court) to do any of the following:

- carry on business for more than four weeks after the making of the winding-up order;
- pay any class of creditors in full;
- compromise claims by or against the company; and
- appoint solicitors to assist in his or her duties.

Court sanction is required for any member of the committee of inspection to receive payment for services rendered by him or her in connection with the administration of the assets, or for any goods supplied by him or her to the liquidator for or on account of the company. Such sanction may only be ordered where the service performed is of a special nature. In addition, the express sanction of the court is required for the payment of any remuneration to a committee member for services rendered by him or her in the discharge of the duties attaching to his or her office as a member of such committee.

In a judicial management, the creditors may appoint a committee to supervise the judicial manager. This committee cannot interfere with the management of the company, but may require the judicial manager to furnish it with such information as it may require.

#### **Insolvency of corporate groups**

##### **29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

As each member of a corporate group is a separate legal entity, insolvency proceedings involving companies within the corporate group proceed separately. The assets and liabilities of each company within

a corporate group are also dealt with separately. Assets can be transferred from a company in liquidation with a branch in Singapore to the main liquidation overseas, but this is subject to the assets in Singapore being used to settle all liabilities in Singapore first (see question 47).

#### **Appeals**

##### **30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

Court orders made in an insolvency proceeding may be appealed as of right. Generally, there is no specific requirement to post security in relation to such an appeal.

#### **Claims**

##### **31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

Once a winding up has commenced, the liquidator will issue a notice calling on the company's creditors to lodge a proof of debt on a date specified in the notice (as determined by the liquidator). This date must be at least 14 days after the date of the notice. The notice itself must be made in the following three ways:

- by advertisement in such newspaper as the liquidator thinks is convenient;
- writing to every person who, to the knowledge of the liquidator or judicial manager, claims to be a creditor of the company and whose claim has not been admitted; and
- writing to every person mentioned in the statement of affairs as a creditor who has not proven its debt.

A proof of debt must, in any event, be filed by a creditor within three months after the winding-up order is made.

All debts payable on a contingency, and all claims against the company, present or future, certain or contingent, ascertained or sounding only in damages, are admissible to proof against the company. Upon receiving the proofs, the liquidator then assesses the proofs. Where the value of the debt does not bear a certain value, the liquidator may make a just estimate of it. A creditor who is dissatisfied with the decision of the liquidator may appeal to the court.

A creditor proving his debt shall deduct therefrom all trade discounts, but he shall not be compelled to deduct any discounts, not exceeding 5 per cent on the net amount of his claim, which he may have agreed to allow for payment in cash.

Interest can be claimed by a creditor up to the rate of 5.33 per cent per annum from the time when the debt or sum was payable until the time of payment.

#### **Modifying creditors' rights**

##### **32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

The priority of creditors claims are governed by the Act, and the court may not change the rank of a creditor's claim. Pursuant to section 300 of the Act, all unsecured property of a company must be applied *pari passu* in satisfaction of its liabilities.

#### **Priority claims**

##### **33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Secured creditors need not prove their debts but can realise their security and obtain full satisfaction. If the security is inadequate, they may prove as unsecured creditors for the balance.

For unsecured creditors, the Act provides that the following preferential debts have priority (in the order set out below) over a floating charge holder and over other unsecured creditors, in order of priority:

- costs and expenses of the winding up;
- wages and salaries of employees up to a maximum of five months' salary or S\$12,500 (whichever is less), with the remainder being an unsecured debt;
- retrenchment benefits and ex gratia payments under the Act up to a maximum of S\$12,500, with the remainder being an unsecured debt;
- compensation to an employee for injuries suffered in the course of employment under the Work Injury Compensation Act;
- amounts due in respect of contributions payable during the 12 months before, on or after the commencement of the winding up by the employer of any person relating to employees' superannuation or provident funds;
- remuneration in respect of holiday leave;
- taxes; and
- gratuity and retrenchment benefits under the Employment Act.

The cap of five months' salary or S\$12,500 applies to the total amount of wages or salaries and retrenchment benefits or ex gratia payments that may be due.

#### Employment-related liabilities in restructurings

##### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

In a liquidation, various employee claims are classed as preferential debts. See question 33.

#### Pension claims

##### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

Pension-related claims against employers in insolvency proceedings are granted priority under the Act if the pension is an approved scheme under Singapore law. Such claims are granted priority as long as they are payable during the 12 months before, on or after the commencement of the winding up by the employer.

#### Environmental problems and liabilities

##### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

There is no legislation in Singapore which relates to responsibility for environmental problems caused by companies specifically involved in insolvency proceedings. Generally, legislation which relates to environmental issues accords the relevant government authorities with broad powers to require any person (which would include any company or association or body of persons, corporate or unincorporated) who has caused the environmental problem to remediate the damage caused. As such, the relevant government authority could require the insolvency administrator in charge of the insolvent company or any other third party that had caused the environmental problem to remediate the damage caused (see for example, section 18 of the Environmental Protection and Management Act).

The environmental-related legislation also generally imposes personal liability on any person (be it an insolvency administrator, officers or directors of the company or otherwise) who has committed an offence and/or is complicit in the commission of an offence as stipulated under the relevant legislation.

#### Liabilities that survive insolvency proceedings

##### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

No liabilities will survive the liquidation and dissolution of an insolvent company. Similarly, in the case of a scheme of arrangement, no liabilities of any creditors will survive if all payments are successfully made pursuant to the scheme (although an unliquidated tort claim covered by insurance may be an exception to this rule): *SAAG Oilfield Engineering (S) Pte Ltd (formerly known as Derrick Services Singapore Pte Ltd) v Shaik Abu Bakar bin Abdul Sukol* [2012] SGCA 7.

#### Distributions

##### 38 How and when are distributions made to creditors in liquidations and reorganisations?

This question is relevant only for liquidations. A liquidator may, from time to time, declare interim dividends. Once he or she has fully realised all the company's assets, a final dividend will be declared. In either case, before declaring a dividend, the liquidator must give notice of his or her intention to do so. The notice is to be made no more than two months before the declaration. It is to be published in the gazette, and written notice must be sent to every creditor mentioned in the statement of affairs who has not proved its debt.

#### Transactions that may be annulled

##### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

A liquidator and a judicial manager have the power to set aside unfair preferences and transactions at an undervalue given when a company was insolvent or as a result of which the company became insolvent. A transaction at an undervalue can be challenged if it took place within five years before the presentation of a winding-up application. An unfair preference which is not also a transaction at an undervalue and which is given to an associate of the company can be challenged if it took place within two years before the presentation of the winding-up application. Any other unfair preference can be challenged if it took place within six months before the presentation of the winding-up application.

A floating charge on the undertaking or property of a company created within six months of the commencement of the winding up is invalid except to the amount of any cash paid to the company at the time of or subsequently to the creation and in consideration of the charge together with interest on that amount at the rate of 5 per cent per annum unless it can be proved that the company was solvent immediately after the creation of the charge.

A liquidator is empowered to recover the excess consideration or excess value received by directors of a company on a sale to or purchase from the company of property for a consideration other than shares occurring within the two years before the commencement of the winding up. Where what was sold to the directors is a business, the liquidator can also recover any goodwill or profits that might have been made from the business.

Any security created by a registrable but unregistered charge is void against the liquidator of the company or any creditor of the company.

Dispositions of the property of the company, including things in action, and any transfer of shares or alteration in the status of the members of the company made after the commencement of the winding up by the court will be void, unless the court orders otherwise. Conveyances of property with intent to defraud creditors are also voidable.

#### Proceedings to annul transactions

##### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

Voidable transactions may only be attacked by a liquidator or judicial manager, with the exception of transactions defrauding

### Update and trends

As part of the Ministry of Law's ongoing review of the insolvency laws of Singapore, the Insolvency Law Review Committee was appointed in late 2010 to review the existing bankruptcy and corporate insolvency regimes. The committee issued its final report in 2013, wherein it recommended the enacting of a new omnibus Insolvency Act that would consolidate and update the core areas of Singapore's bankruptcy and corporate insolvency laws. The Ministry of Law has also obtained public feedback on the report, where general consensus regarding the new omnibus Insolvency Act was received. We understand that the relevant authorities are currently preparing the draft of the omnibus Insolvency Bill. The reforms include, among others, allowing for super-priority for rescue financing, cram-down provisions

similar to those in US Chapter 11 proceedings, judicial management being made available to foreign companies and the adoption of the UNCITRAL Model Law on Cross-Border Insolvency.

In addition, a second committee was formed in 2015 (the committee to strengthen Singapore as a restructuring hub) to facilitate cross-border restructurings in Singapore. The recommendations include, among others, super priority liens, an automatic one-month moratorium when a scheme of arrangement is applied for, the moratorium being extraterritorial to the extent that it restrains creditors subject to the jurisdiction of the Singapore courts. Further, to facilitate a group restructuring, injunctive relief may be obtained to restrain proceedings against related entities.

creditors, which may be attacked by any person thereby prejudiced. See question 39 regarding the relevant time periods.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

While the company's directors and officers are not generally personally liable for their corporation's obligations, they may be held personally liable if they have breached certain provisions in the Act. For example, breach of directors' fiduciary duties to the company under section 157; wrongful trading under section 339(3); or fraudulent trading or misfeasance under sections 340 and 341 respectively. See question 13 for more information.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Parents and affiliated corporations are treated as separate legal entities and as such will, in the majority of cases, not be held responsible for the liabilities of their subsidiaries or affiliates unless the court is of the view that the corporate veil of the companies should be pierced. This would only be done in exceptional circumstances such as when the corporate veil is a mere facade that is concealing the true facts, or when the group is essentially trading or acting as one company. While it is possible in theory, it is unlikely that a court will order a distribution of group company assets pro rata in the absence of strong reasons to pierce the corporate veil of the companies involved.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

No, there are no such restrictions insofar as those transactions from which the claim arises are not an unfair preference or transactions at an undervalue (see question 39 above).

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

A debenture holder may have the power, pursuant to a provision in the debenture, to appoint a private receiver and manager. Similarly, a legal mortgagee's power of sale can be exercised without resort to court provided the conditions under the mortgage for its exercise have arisen. A court order is necessary only if the mortgagor refuses to give up possession of the land voluntarily or if the lender wishes to foreclose instead of exercising his power of sale.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

If a company is not carrying on business or is not in operation, the Registrar of Companies may order that it be struck off the Register of Companies after sending or publishing the requisite notices. The company is dissolved upon the publication of the notice of dissolution in the gazette. The assets of the company, if any, are vested in the official receiver.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

At the end of a successful judicial management, if the objectives have been achieved the company will emerge from judicial management and carry on business. However, if the judicial management is unsuccessful, the judicial manager will apply to the court for the company to be wound up and a liquidator will be appointed.

In a court-ordered liquidation, the liquidator may apply to the court to be released and the company dissolved when he or she has realised the property of the company and issued a final dividend, if any.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

Singapore is not a party to any international treaties with regard to cross-border corporate reorganisation and rescue matters. There is also no special statutory provision in Singapore that deals with cross-border insolvency, reorganisation and rescue issues. The adoption of the UNCITRAL Model Law on Cross-Border Insolvency has been recommended for adoption in Singapore in the future.

If a foreign company goes into liquidation in its place of incorporation or origin, it may be concurrently wound up in Singapore and a liquidator for Singapore will be appointed by the court. If the foreign company is registered in Singapore or has or intends to carry on business in Singapore, the liquidator may only recover and realise the assets of the foreign company in Singapore and must pay the net amount recovered and realised to the foreign liquidator after paying any debts and satisfying any liabilities incurred in Singapore by the foreign company. In paying off the foreign company's debts and liabilities in Singapore, the Singaporean regime for priority of debts will apply (*Tohru Motobayashi v Official Receiver & Another* [2000] 4 SLR 529). This ring-fencing provision does not apply to an unregistered foreign company or a company which does not carry on or intends to carry on business in Singapore (*Beluga Chartering GmbH (in liquidation) & Ors v Beluga Projects (Singapore) Pte Ltd (in liquidation) & Anor (deugro (Singapore) Ptd Ltd, non-party)* [2014] SGCA 14 (*Beluga Chartering*)).

If an insolvent foreign company, whether registered or not, is not concurrently wound up in Singapore, the application of the ancillary liquidation doctrine does not arise and any issues that arise before the Singapore courts would instead involve questions of recognition (ie, the recognition of the title of the foreign liquidator and the recognition of the foreign proceedings). Whether and how the Singapore court will render assistance to foreign winding up proceedings will depend on the circumstances of each case (*Beluga Chartering*).

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#### COMI

**48** What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

The concept of COMI is not generally recognised in this jurisdiction. However, in *Re Opti-Medix Ltd (in liquidation)* [2016] SGHC 108, the Singapore High Court recognised a Japanese bankruptcy trustee's powers over a company incorporated in the British Virgin Islands, with operations in Japan based on the application of COMI principles. See question 47 on the ring-fencing of assets.

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#### Cross-border cooperation

**49** Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

See question 47.

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#### Cross-border insolvency protocols and joint court hearings

**50** In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

There are no cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries. There are no reported decisions of the Singapore courts where the court has communicated with or held joint hearings with courts in other countries in cross-border cases.




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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The Spanish insolvency regime is mainly governed by the Spanish Insolvency Act (Law 22/2003, dated 9 July 2003) but has been the subject of several amendments, the latest being in October 2015. The Insolvency Act establishes a single insolvency proceeding applicable to both individuals and corporates, providing for the possibility of a settlement agreement between the debtor and its creditors and, if agreement is not reached, for the liquidation of the debtor's assets towards the payment of creditors.

In addition to the Insolvency Act, the following pieces of legislation, among others, are relevant in the context of an insolvency:

- the Civil Procedure Act;
- the Securities Market Act;
- the Recovery and Resolution of Credit Institutions and Investment Services Firms Act;
- the Supervision and Solvency of Insurance and Re-insurance Companies Act; and
- the Companies Act.

Cross-border EU insolvencies are governed by Council Regulation (EC) No. 1346/2000 and Regulation (EU) 2015/848 of the European Parliament and of the Council on insolvency proceedings.

Under the Insolvency Act, the only criteria to determine if a debtor is insolvent is a cash-flow test, with a debtor being considered insolvent when it is unable to regularly meet its payment obligations when they fall due.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Commercial courts have exclusive jurisdiction to hear insolvency proceedings. The relevant commercial court to which the insolvency is allocated will retain jurisdiction over most of the disputes that may arise during the insolvency proceedings, for as long as such disputes affect the debtor's assets and rights. In addition, the relevant commercial court will not only hear insolvency claims against the debtor but also certain labour claims arising from the insolvency (eg, termination, amendment and suspension of labour contracts), transaction avoidance claims, claims for directors' liability and attachment of the debtor's assets.

Pursuant to the Insolvency Act, other court proceedings pending in the courts of first instance can be transferred to the commercial court at the time of the filing for insolvency if the dispute is considered to be relevant for the preparation of the assets' or the creditors' list.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

The only entities that are excluded from the Insolvency Act are public administrations and other public entities. In addition, there are some

particular rules applicable to financial entities, insurance and reinsurance companies (see question 1) establishing specific provisions affecting certain types of transactions and these institutions.

Certain items (such as furniture, clothes, food, sacred objects or a certain amount of the salary, where the debtor is a natural person) are excluded from insolvency proceedings. Claims against assets that are encumbered with an in rem security in favour of the secured creditor are limited. Finally, specific rules apply to financial collateral that complies with the Spanish regulation that implements the Financial Collateral Directive.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The determining criterion for entities to be considered immune from insolvency is that they must be deemed to have *personalidad jurídico-pública* (public legal personality). Therefore, as indicated in question 3 above, public administrations and other public entities which have such public legal personality cannot be declared insolvent since they exist to serve public interests and their assets are considered unseizable.

However, government-owned entities that do not have the above-mentioned public legal personality (eg, public corporate companies and the majority of foundations) may be declared insolvent irrespective of whether they are government-owned. For these entities, there is no special regime or procedure to be followed within an insolvency scenario and therefore the general rules set out in the Insolvency Act apply.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Yes. Law 9/2012 on restructuring and resolution of credit institutions was enacted to provide the Spanish supervisory authorities with certain tools, powers and procedures to tackle the risk of systemic failures and, more generally, reinforce their ability to deal with Spanish credit institutions in financial distress.

Law 9/2012 has been partially derogated by Law 11/2015 on the Recovery and Resolution of Credit Institutions and Investment Services Firms, which entered into force on 20 June 2015 (save for certain provisions that entered into force on 1 January 2016 and some others that will enter into force on 3 July 2017). Law 11/2015 implements Directive 2014/59/EU of the European Parliament and the Council, and it is based on identical principles to Law 9/2012.

Law 11/2015 contemplates two possible procedures – early action and resolution – whose application mainly depends on the viability of the credit institution in financial difficulty and on whether it requires bailout funds to survive. These procedures constitute an alternative to normal insolvency proceedings under the Insolvency Act and ultimately intend to provide a means to restructure or wind down Spanish credit institutions that are failing or likely to fail and whose failure would create concerns in terms of general public interest. In the absence of such general public interest, Spanish credit institutions may be allowed to fail in the ordinary way (ie, through normal insolvency proceedings).

The main changes introduced by Law 11/2015 are:

- the reinforcement of the preventive phase of the resolution by requiring all credit institutions (and not only those that are not economically viable) to have recovery and resolution plans;
- that the absorption of losses (bail in) will affect all types of creditors (and not only subordinated creditors);
- new regime of maximum protection of depositors; and
- the creation of a specific resolution fund funded by contributions from the private sector. Law 11/2015 has been further developed by Royal Decree 1012/2015.

### Secured lending and credit (immovables)

#### 6 What principal types of security are taken on immovable (real) property?

The main security over immovable property is the mortgage, regulated in articles 1,874 to 1,880 of the Civil Code and in the Mortgage Act.

A mortgage is an in rem security whereby real estate assets that are subject to registration (and certain transferable rights attached thereto, such as usufruct rights and administrative concessions) are charged as security for the fulfilment of a monetary obligation.

Mortgages must be granted in a public deed before a notary public and be registered with the appropriate Land Registry. No security enforceable against third parties is created until the registration of the mortgage has been completed.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The main security over moveable property is the pledge, which is regulated by articles 1,863 to 1,873 of the Civil Code.

A pledge is an in rem security whereby possession over certain moveable assets is transferred to the pledgee (or to a third party that acts as depositary) as security for the fulfilment of the secured obligation. Therefore, the owner of the pledged asset, although losing possession, does not transfer title.

To be enforceable against third parties, pledges must generally be granted in a public document (either in an *escritura* or a *póliza*) and possession over the pledged asset must be transferred either to the pledgee or to a depositary. Specific provisions apply to pledges over credit rights and other moveable properties.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Creditors may file an application with the relevant court requesting the granting of interim measures for as long as these are deemed appropriate to ensure that the final judgment, should it be in favour of the creditor, can be effectively enforced.

Creditors have access to specific interim measures (eg, seizures, preventive registration of the claim in the relevant public registry, deposit of assets), as well as all the interim measures that are generally available by statute. Often interim measures are requested by creditors in insolvency situations where there is a concern that the debtor is concealing its assets.

Interim measures can be applied for prior to, together with or after the filing of the claims and can be granted with or without previously hearing the defendant by providing evidence that the general requirements are met, these being:

- the applicant's claim appears to have some merit;
- a fear that the delay of proceedings may lead the defendant to conceal or sell its assets; and
- the provision of a cross-undertaking in damages to cover the potential damages that the interim measures may cause.

In general terms, foreign creditors are subject to the same regulations and have the same rights as Spanish creditors.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

The Spanish Companies Act provides for a voluntary liquidation of the company. This process is different to an insolvency process.

A voluntary liquidation is commenced when the company is solvent but a winding-up cause occurs. Winding-up causes can be set out in the company's articles of association or be triggered under Spanish corporate legislation. For example, a winding up-cause is established where the company's losses have reduced its equity to below 50 per cent of its share capital (unless the share capital is restored).

If a winding-up cause occurs, directors must call a general shareholders meeting to request that a winding-up resolution is passed. Where the directors fail to call the general shareholders' meeting or the shareholders fail to pass a resolution to wind up the company (and the winding-up cause is not cured) any interested party can and the directors of the company must, apply to the commercial court to initiate winding-up proceedings.

The effects of the voluntary liquidation resolution will depend on the type of company concerned. Most Spanish companies are either corporations or limited liability companies. The effects of voluntary liquidation on these two entities are broadly the same: the company's directors will no longer have authority to manage the company and one or more liquidators will be appointed at the general shareholders' meeting. The liquidators will be charged with, inter alia:

- collecting the company's debts and realising the company's assets;
- paying the company's creditors;
- concluding any outstanding commercial transactions; and
- entering any new transactions that may be necessary for the company's liquidation.

The liquidator must also prepare the liquidation balance sheet, which may be challenged by the company's shareholders. At the end of the period for challenging the balance sheet, if no challenges have been made or if a challenge has been made and a final judgment has been issued, the company's remaining assets (after payment of all creditors) will be distributed to the shareholders.

See question 13 in relation to directors' duties to file for insolvency.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Creditors can apply to the court to place a debtor into an insolvency process. For creditors to apply for insolvency they will need to either:

- satisfy the court with evidence showing that they have unsuccessfully attempted execution proceedings against the debtor's assets (and have found it impossible to attach any assets from which to obtain payment); or
- provide evidence that:
  - the debtor has generally ceased making payments;
  - the debtor's assets have been seized;
  - the debtor is selling its assets very fast or in a harmful way; or
  - there is a breach of certain payment obligations (ie, taxes, social security wages or salaries) for at least three months.

If a creditor files an application for the debtor's insolvency with the court, the debtor can either agree to the creditor's request or reject the creditor's request within five working days. If the debtor rejects the request it is required to deposit the amount of the debt owed to the creditor applying for insolvency (if it is due and payable) with the court. If the debtor refuses to deposit the amount with the court, the judge would hear representations from the parties on whether the insolvency declaration is appropriate. The parties will then be called to a hearing after which the court will render a decision on whether to declare the insolvency.

The effects of the creditor initiating insolvency proceedings are broadly the same as in the case where the directors file for insolvency, as set out in question 13.

A certain percentage (50 per cent) of the debt owed to the creditor applying for insolvency will hold a general privilege (provided that such debt does not qualify as subordinated), which may be an incentive for

unsecured creditors to file for insolvency (see question 33 on the ranking of debts).

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Voluntary reorganisations can take place through ‘refinancing agreements’. These can be either: individual refinancing agreements; collective refinancing agreements or court-sanctioned collective refinancing agreements.

An individual refinancing agreement is a notarised agreement that satisfies the following conditions:

- it improves the ratio of assets over liabilities;
- it ensures that the current assets are no less than the current liabilities;
- the value of the security interests (calculated in accordance with Insolvency Act provisions) is not of a greater proportion of the outstanding debt owed to creditor than of the debt prior to the refinancing; and does not exceed 90 per cent of the value of the outstanding debt owed to such creditors;
- it does not increase the interest rate applicable to the debt by more than one-third of the interest rate applicable to the debt prior to the refinancing; and
- it expressly states the reasons that justify, from an economic point of view, the terms of the refinancing, making specific reference to each of the above conditions.

A collective refinancing agreement is a notarised agreement which satisfies the following conditions:

- it has the support of creditors whose claims represent at least three fifths of all the debtor’s indebtedness; and
- it extends maturity dates, grants new credit or replaces financial obligations or a combination of these, in each case, in accordance with a viability plan that allows business activity to continue in the short and medium term.

In the case of syndicated loans, all syndicated lenders shall be deemed to have supported the collective refinancing agreement if such refinancing agreement is approved by lenders representing at least 75 per cent of the financial indebtedness under the syndicated loan, save where the parties to the syndicated loan have agreed to a lower threshold, in which case the lower threshold shall apply.

A court-sanctioned collective refinancing agreement is an agreement that satisfies the following conditions:

- it meets the criteria set out above for a collective refinancing agreement;
- it has the support of creditors whose claims represent at least 51 per cent of the debtor’s financial indebtedness; and
- it has received the sanction of the court as to compliance with requirements set out above (such sanction is called ‘homologation’).

To determine whether the 51 per cent threshold has been satisfied, the following rules apply:

- financial indebtedness held by creditors considered to be related parties is not taken into account, although these creditors may nevertheless be bound by the judicially sanctioned agreement;
- all holders of any financial debt (excluding commercial transaction creditors, creditors for labour credits and creditors for public law liabilities) are considered creditors of financial indebtedness, regardless of whether they are subject to financial supervision; and
- in the case of a syndicated loan, all of the lenders shall be taken to have supported the judicially sanctioned agreement if such agreement is approved by lenders representing at least 75 per cent of the financial indebtedness under such syndicated loan, save where the parties to the loan have agreed to a lower threshold, in which case the latter shall apply.

A court-sanctioned refinancing agreement is the only type of refinancing agreement that can bind dissenting (including absentee) unsecured and secured creditors of financial indebtedness in relation to the debtor provided that the required majorities set out in the Insolvency Act approve it.

A judicially sanctioned agreement may only be challenged by a dissenting creditor if the relevant required majority has not been obtained or if the refinancing agreement imposes a ‘disproportionate sacrifice’ on the creditor. There is no legislative guidance on what constitutes ‘disproportionate sacrifice’. Any such challenge must be brought within 15 days of the publication of the judicial sanction.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Creditors cannot commence an involuntary reorganisation. Creditors can, however, initiate insolvency proceedings (see question 10 for the requirements and effects).

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

The directors must initiate insolvency proceedings within the two months following the date on which they knew or should have known that the company was insolvent. A debtor is considered to be insolvent when it is not able to meet regularly its payment obligations as they fall due (see question 1). Breach of this obligation may result in the insolvency being classified as a ‘guilty insolvency’ in the qualification phase of the insolvency proceedings (see below).

The two-month period can be extended by up to an additional four months by means of an article 5-bis filing.

In order for the debtor to apply for insolvency, it must provide evidence to the court of the amount of its debts and its present or immediate insolvency situation. The following documents must be attached to the application:

- a special power of attorney granting the court representative the authority to request the insolvency;
- a report including economic and legal details of the three preceding years, the premises, offices and all assets owned by the debtor, the factors causing the debtor’s current situation, a complete valuation of the debtor’s assets, liabilities, etc, proposals for its economic viability, the identification of the shareholders, directors or liquidators, auditor, the companies that form part of the same group (if any) and whether the company is listed;
- an inventory of assets and rights expressing the nature of the asset, place of location, registry identification data, acquisition value, estimates of current value, attachments, seizures and charges;
- a list of creditors, including identity, amount, maturity, personal or in rem securities granted and any current judicial proceedings;
- the annual accounts, managing reports and auditors’ reports of the past three years;
- the details of any significant changes in the debtor’s assets that have taken place post-closing of the annual accounts and of any other operation not in the ordinary course of business (because of its nature, object and amount);
- a list of the employees and, as the case may be, identification of the workers’ representatives;
- a report of the operations carried out between members of the debtor group in the past three years; and
- an anticipated settlement proposal (if any).

The relevant court will issue the insolvency order provided that the above requirements are met ordering the registration of the insolvency order in the relevant commercial and land registries. The order declaring the opening of the insolvency proceeding shall be published on the Public Insolvency Register and in the Spanish Official Gazette.

The main consequences of the debtor initiating insolvency proceedings are as follows:

- The court will issue an insolvency order declaring whether the requirements for opening insolvency proceedings have been met and will appoint an insolvency receiver who will provisionally be in charge of managing the debtor’s assets and activities. It is possible that the directors will continue to manage the business but under the supervision of the insolvency receiver. Whether directors are

entirely released from their duties or continue in office under the supervision of the insolvency receiver will be at the court's discretion in view of the particular circumstances of the case. In some cases, the court may appoint a second insolvency receiver.

- The debtor must not enter into any new transactions, unless approved by either the insolvency receiver (where the directors have been released from their duties) or the directors with the authorisation of the insolvency receiver (in the event of supervision of the directors). In each of these cases, the court will have to analyse the relevant transaction and authorise it. Several transactions are carved out from this prohibition including disposals that the insolvency receiver considers indispensable to secure the viability of the company, disposals of assets that are not necessary for the continuity of the company's activity and disposals of business units, in each case, subject to certain conditions.
- Accrual of interest is suspended as of the date of the declaration of the insolvency except for those credits secured with rights in rem up to the maximum covered by the security.
- Contracts are maintained: insolvency is not a valid cause for termination of a contract. For agreements where reciprocal obligations were pending at the time of the insolvency declaration, the insolvency receiver can request their termination if such termination is beneficial for the insolvency estate (see further question 21).
- Apart from certain exceptions mentioned below (see question 15), attachment proceedings against the debtor's assets can neither be initiated nor continued.

There are two phases in an insolvency process; the first phase is aimed at determining the debtor's assets and liabilities and the second phase may lead to either an arrangement between the debtor and its creditors or a liquidation of the debtor's assets to satisfy creditors. In addition, there is a 'qualification phase'. This is aimed at investigating the potential liability of directors, accomplices and shareholders. The qualification phase is opened automatically when:

- a settlement inclusive of a delay in the maturity of debts of more than three years or a waiver to more than one third of the amount of the debts is approved;
- a previous settlement agreement is breached; or
- the liquidation phase is opened.

The insolvency proceedings shall be classified as involuntary or guilty. The consequences of the guilty classification may include:

- disqualification of the directors from managing third-party assets or representing or managing any person or company for a period from two to 15 years;
- removal of the directors' rights as creditors of the debtor;
- return of the directors' rights or assets that were unduly obtained from the debtor;
- payment of indemnities for any loss or damage caused; and
- (in certain circumstances) the directors are held liable for the payment of any deficit to the creditor.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

Depending on the particular circumstances of the case, the court may, in its insolvency order, state that the debtor's directors are released from their duties or order that the directors continue in office under the supervision of the insolvency receiver. There is a preference for releasing the directors if the insolvency filing is made by a creditor.

The mere declaration of insolvency does not trigger suspension of the commercial activities of the debtor. Moreover, the Insolvency Act envisages that the insolvency receiver may provide directors with a general authorisation to enter into certain operations, notwithstanding their obligation to report all the operations entered into by the debtor to the insolvency receiver. The debtor or the insolvency receiver (where the debtor's directors are released from their duties) are able to sell

assets if, among others, this is within the debtor's ordinary commercial activities; or otherwise, provided that the court has authorised such sales subject to certain exceptions (see question 13).

The winding up of the business can only be agreed by the court at the request of the receiver and having previously heard the employee representatives.

Claims in relation to goods supplied or services rendered to the debtor will be considered as debts of the insolvency estate and will have full preference in payment over any other claim, other than specially privileged claim) (see question 33).

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

Any declarative proceeding (ie, seeking an order declaring a certain right, requiring the debtor to pay a certain amount or ordering the debtor to do something or to refrain from doing something) pending at the time of the insolvency declaration will continue except for those proceedings regarding damages caused by the debtor's directors, liquidators or auditors, which will be accumulated ex officio as long as these are at first instance and the hearing has not been held. New declarative proceedings can be initiated but must be filed with the insolvency court.

Any unsecured claim for the attachment of assets ongoing at the time of the insolvency declaration can continue in certain circumstances, provided that the assets attached are not required to continue running the business. No new unsecured claims for the attachment of assets can be initiated during the insolvency proceedings.

Security over the assets that are necessary for the continuity of the debtor's business cannot be enforced until a settlement agreement that does not affect the security or secured claim is approved, or a year elapses since the insolvency declaration without the liquidation phase being opened. The enforcement of security interests over the shares of ring-fenced and self-standing special purpose vehicles is not suspended provided certain requirements are met.

In addition, the moratorium does not apply to secured claims over assets that are not related to the business or to certain 'financial collateral'. The determination as to whether the assets encumbered are related to the business of the insolvent company will be made by the commercial court in charge of the insolvency proceeding.

Further, during the additional period to file for insolvency following the filing under article 5-bis (see question 13) any existing enforcement actions over assets and rights necessary for the continuity of the business will be suspended and the creditors will be prevented from commencing any enforcement action against these assets and rights. During this period, no enforcement will be possible by financial creditors over any of the assets if financial creditors holding at least 51 per cent of the indebtedness owed to such creditors have expressed their support for the commencement of refinancing negotiations and have agreed not to initiate (or continue with) enforcement proceedings. Enforcement by secured creditors will be permitted but will be suspended as from the article 5-bis filing.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

The Insolvency Act does not expressly regulate the debtor's right to obtain secured or unsecured loans but provides that during the insolvency proceedings it is possible to resume loan agreements that have been accelerated in the three months prior to the insolvency declarations (ie, acceleration will be of no effect and the parties' obligations under the contract will be restored).

The creditor's claims will be deemed to be debts of the insolvency estate and will have full preference in payment over any other insolvency debt other than specially privileged claims (see question 33).

If new money is granted by a party that is not related to the debtor within the context of a refinancing agreement or a court-sanctioned agreement, 50 per cent of the principal amount would be treated as claims against the estate (in broad terms, ranking alongside the insolvency receiver's fees and ordinary course of business-related costs of

the debtor necessary to maintain the business activity during the insolvency proceedings). The remaining 50 per cent of the principal amount of the new money would be treated as generally privileged. Separately all new money granted (including by a party related to the debtor) pursuant to any refinancing agreement entered into on or before 2 October 2016 shall, for a period of two years from the granting of such new money, be treated as preferred claim. New money provided by means of a capital increase is excluded.

### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

In general, set-off is not permitted in an insolvency proceeding unless the requirements for set-off have been met prior to the insolvency declaration.

As an exception to the general regime, set-off provisions that comply with the requirements set out in Royal Decree-Law 5/2005 (which implements EU Directive 2002/47 on financial collateral) will be enforceable in an insolvency scenario.

Set-off is allowed if the claim is not governed by Spanish law and where the applicable law allows such set-off in insolvency proceedings, subject to certain limitations.

### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

During insolvency proceedings both specific assets and business units may be sold subject to the regime summarised below:

During the common phase, the sale of assets can only be completed with the prior authorisation of the insolvency judge, except where the insolvency administrator determines that such sale is required to sustain the continuation of the insolvent company and the sale is subsequently communicated to the judge.

Depending on the phase of the insolvency proceedings, the decision as to whether the sale of a specific asset or business unit needs to be disposed of lies with the insolvency administrator (subject, as the case may be, to the approval of the judge as discussed above) or the liquidator, in cases where the liquidation phase has been opened and subject to the terms of the relevant liquidation plan, which has to be approved by the judge.

Generally, and except in circumstances where the urgency of the sale advises otherwise, the insolvency receiver or liquidator will try to maximise the proceeds of any such sale by establishing auction processes, where credit bids are allowed. In these auctions not only the bid price but also criteria such as the continuation of the business, the preservation of employment and the solvency of the bidder will be taken into consideration.

The sale of business units may take place during the first or the second phase of the insolvency proceedings, subject to the following rules:

- The sale of a business unit shall imply the transfer (without requiring the consent of the counterparty) of the rights and obligations arising from any agreements that are attached to the continuity of the relevant professional or business activity (unless their termination has been requested in the framework of the insolvency proceedings).
- The sale of a business unit shall also imply the transfer of any administrative licences or authorisations that are attached to the continuity of the relevant professional or business activity, to the extent the purchaser carries on the relevant activity in the same premises.
- The sale of a business unit shall not imply that the purchaser assumes any debt of the insolvent company that remains outstanding at the time of the sale, subject to certain exceptions and unless the purchaser is a related party to the insolvent company.

In the case of liquidation, the following rules apply in respect of secured assets pertaining to a business unit, depending on whether they are transferred free of charges or still subject to the relevant security:

- transfer subject to security: no consent of the relevant secured creditor shall be required; and
- transfer free of charges:
  - creditors shall receive a portion of the purchase price equal to the proportion that the value of the relevant secured asset represents in respect of the total value of the relevant business unit; and
  - if the purchase price to be received is lower than the value of the relevant secured asset, the sale shall require the support of 75 per cent of the secured creditors pertaining to the same class which are affected by the sale.

In addition, where offers do not differ by more than 15 per cent, the judge may award the business unit to the lower offer if it secures to a greater extent the continuity of the relevant business and employment, and also a better satisfaction of the claims of the creditors.

### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

The Insolvency Act does not contain any particular rule with respect to IP assets or contracts over IP assets. By application of the general rules on contracts:

- the mere existence of the insolvency proceedings does not itself allow for termination of a contract;
- contracts may continue in force during the insolvency proceedings but any obligation arising from such contracts for the debtor will be classified as a debt of the insolvency estate and will have full preference in payment over any other insolvency claims (other than specially privileged claims);
- contracts can be terminated in the event of insolvency when one of the parties breaches its contractual obligations; and
- contracts can be terminated by the insolvency receiver if he determines that the termination is beneficial for the debtor.

However, in all cases permitting a termination this must be approved by the court.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Insolvency Act does not contain any particular rule with respect to the use or transfer of personal information or customer data.

By application of the general regulation on personal or customer data (Data Protection Act) the transfer of personal data is only authorised with the consent of the data subject. Nevertheless, Spanish regulations stipulate a series of exceptions to this rule. In particular, Royal Decree 1720/2007 establishes that no data transfer will be deemed to occur in the case of modification of the controller as a result of a merger, spin-off, global transfer of assets and liabilities, contribution or transfer of business or branch of business, or any corporate restructuring operation of a similar nature contemplated by commercial legislation.

**Rejection and disclaimer of contracts in reorganisations**

**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

The insolvency receiver may ask the insolvency court to terminate agreements under which the debtor had pending obligations to be fulfilled if he or she considers that such termination is beneficial for the insolvency proceedings. The basis on which such termination can be agreed is quite open and only requires convenience for the debtor. On termination, the non-insolvent party is entitled to claim damages arising as a consequence of such termination, such damages being considered as a debt of the insolvency estate and with full preference in payment over any other insolvency debt (except for specially privileged claims). For more information of the ranking of the debts of the insolvency estate please see question 33.

In addition, if the debtor breaches the agreement after the insolvency declaration, the counterparty is entitled to ask the insolvency court to terminate it, based on the breach. However, even if a cause for termination concurs, the court may decide not to terminate the agreement in the interests of the insolvency estate. In such a case, the debtor's obligations that may arise will be considered as a debt of the insolvency estate.

The above is without prejudice to other clawback remedies, as described in question 39.

**Arbitration processes in insolvency cases**

**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

In general terms, arbitration clauses will continue to be effective, with the Insolvency Act not limiting the types of insolvency disputes that may be subject to arbitration. However, the insolvency court may suspend the effect of arbitration clauses if the court considers these to damage the insolvency proceedings.

Ongoing arbitration proceedings will, however, continue, but the insolvency receiver may stand in for the debtor in such arbitration proceedings.

In general terms, cases arising after insolvency has been declared will be arbitrated if an arbitration clause had been entered into between the parties. If one of the parties filed the relevant claim with the insolvency court instead of submitting it to arbitration, the other party could file a plea for motion of jurisdiction and the insolvency court would normally instruct the parties to submit the dispute to arbitration.

**Successful reorganisations**

**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

Settlement proposals may be filed by the debtor or by the creditors, and may consist of:

- a delay in the maturity of debts up to five years or a waiver for to up to half the company's debts (these limits may be exceeded if the settlement agreement is supported by the 65 per cent of the ordinary claims);
- alternative proposals to all or some classes of creditors except for public creditors (see question 33 for a description of the classification of creditors), such as the conversion of the debt into equity; or
- proposals for the sale of certain assets or business units, but not the winding up of the company (see question 18).

The debtor can make an advanced settlement proposal aiming for a kind of 'pre-packaged' reorganisation, which can be filed from the date when the debtor files for insolvency until the term for the creditors to

communicate their claims has expired. Such advance settlement must be agreed by creditors holding at least one-fifth of the total debts before it can be filed.

Settlement proposals must include a plan for the payment of the debts and, if they foresee the continuation of the business, a business viability plan. The Insolvency Act prohibits any proposals for settlement that consist in the amendment of the priority of the creditors and limits the assignment of assets to the creditors to cases where those assets are not necessary for the debtor's business and whose fair value (calculated according to the Insolvency Act) is equal or less than the value of the credit extinguished. The Insolvency Act does not regulate whether the settlement proposal can include a release of third-party liability.

Settlements must be approved by a majority of creditors. Pursuant to an amendment made by Law 9/2015, the majorities required for the approval of settlement agreements and their extension to dissenting and abstaining creditors are as follows:

	To bind non-privileged creditors	To bind privileged creditors
<b>Full payment of ordinary claims within a term of up to three years</b>	Votes in favour exceeding votes against	
<b>Immediate payment of any due and payable ordinary claims with a discharge lower than 20 per cent</b>		
<b>Discharge up to 50 per cent</b>	50 per cent of ordinary claims	60 per cent of claims within the same class*
<b>Moratorium up to five years</b>		
<b>Conversion into profit participating loan (PPL) for a term of up to five years (except for public or employee claims)</b>		
<b>Discharge above 50 per cent</b>	65 per cent of ordinary claims	75 per cent of claims within the same class
<b>Moratorium up to 10 years</b>		
<b>Conversion into PPL for a term of up to 10 years (except for public or employee claims)</b>		

\* Law 9/2015 introduces the concept of class for privileged creditors, which are now divided into four classes: employee creditors, public creditors, financial creditors and other creditors

The following rules apply to the calculation of majorities:

- in the case of syndicated debt, all syndicated creditors are deemed to have voted in favour if creditors representing at least 75 per cent do so (unless the relevant syndication arrangements contemplate a lower majority, in which case the lower majority applies);
- in the case of creditors with a special privilege (ie, secured creditors), majorities shall be calculated in light of the proportion that the aggregate value of the security held by all the secured creditors supporting the settlement proposal represents compared to the total value of the security granted in favour of creditors pertaining to the same class; and
- in the case of creditors with a general privilege, majorities shall be calculated in light of the proportion that the privileged claims supporting the settlement proposal represents compared to the total amount of the privileged claims of the creditors pertaining to the same class.

Law 9/2015 included several rules for the calculation of the value of secured assets (which are similar to those introduced by Law 17/2014 for refinancing agreements). The portion of secured claims exceeding the value of the underlying secured assets does not qualify as specially privileged.

Upon approval of a settlement the court grants creditors who have not attended the meeting or who have voted against the settlement proposal the opportunity to oppose it. The settlement approved by the relevant majority of creditors and accepted by the court will be binding on the creditors that approved it, on any ordinary and subordinated creditors and on privileged creditors when the majorities set out in the

table above are met (see question 33 for a description of the classification of creditors).

With regard to the release of non-debtor parties, there is no express provision in the Insolvency Act, and, thus, the general regime applies. Therefore, if a creditor agrees to a settlement that foresees a release of a certain amount of debt, such release could also extend, in certain circumstances, to the potential liability of third parties (eg, personal guarantees).

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

Procedures do not exist for expedited reorganisations. Nevertheless, the amendment to the Insolvency Act made pursuant to Law 38/2011 provides for summary insolvency proceedings where procedural terms are reduced to 50 per cent.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

Failure to approve a settlement agreement (or the absence of a settlement proposal) will trigger commencement of the liquidation phase. The purpose of the liquidation phase is to liquidate all the assets of the debtor according to a liquidation plan filed by the insolvency receiver. The debtor and the creditors can comment on the plan so proposed.

In addition, a debtor's breach of the settlement agreement duly approved by the court also triggers commencement of the liquidation phase upon a request being made by the creditors to the insolvency court.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The insolvency declaration is notified to the debtor's creditors that join in the proceedings, is recorded with the relevant commercial registry and the land registries where the debtor's assets are registered and is published in the Spanish official gazette. The court is entitled to order additional measures to give sufficient publicity to the insolvency declaration.

Additionally, the insolvency declaration and any other resolution that, according to the Insolvency Act, must be publicly available, is recorded in the Public Insolvency Registry.

The only meeting held is a creditors' general meeting (if any), during which the settlement proposals, if any, can be discussed and agreed. The Insolvency Act does not regulate the formation of a creditors' committee.

During the insolvency proceedings, a creditor has, among others, the following rights:

- to communicate the amount of the debt and prove it throughout the proceedings;
- to request the termination of certain contracts based on breach of the contractual obligations;
- under certain legal requirements, to exercise some of the remedies attributed to the insolvency receivers (clawback claims);
- to file a settlement proposal;
- to participate in the creditors' meeting and vote for or against a settlement proposal; and
- to apply for liquidation in the event of breach of the settlement.

The creditors' meeting is called by the court and served, through court proceedings, on all those creditors who have appeared at the insolvency proceedings. However, additional publicity can be agreed to by the court, for example, by an announcement in the Official Gazette.

The insolvency receiver has the obligation to prepare, among others, a report on the causes of the insolvency, a list of creditors and a list

of assets and rights. The insolvency receiver also has to prepare a report on the settlement proposal (if any).

As explained in question 23, the effects of settlement agreements may extend to non-privileged or privileged creditors or both to the extent that certain majorities are met. In turn, settlement agreements may not affect the relationship between the creditors and third parties who are not part of the debtor group unless otherwise stated in the settlement agreement and provided that such creditors have voted in favour.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

If the insolvency receiver refuses to exercise a certain remedy, the creditors can exercise such remedy in the interests of the insolvency estate themselves. This means that, if such remedy succeeds, the consequences of the litigation will be attributed to the debtor, but the creditor will have the right to obtain reimbursement of the costs that it incurred against the insolvency estate.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The Insolvency Act does not foresee the possibility of forming a creditors' committee. Creditors are, of course, free to appoint their own counsel or advisers whose fees will be paid by such creditors.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

The Insolvency Act contains specific regulations related to groups filing for insolvency. In particular, the Insolvency Act allows groups of companies to apply together for insolvency proceedings.

The limited liability principle applicable to Spanish companies prevents the assets and liabilities of companies within a group from being combined, although, in some specific cases, it would be possible to perform such consolidation for the purposes of the insolvency receiver's report. This is without prejudice to the fact that intra-group credits are generally subordinated claims and the possibility of (among others) the insolvency receivers challenging those claims if they prejudice the insolvency estate.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

The remedy of appeal is the action to take against a court's decision accepting or rejecting an insolvency petition. This appeal does not have suspensive effect unless the court resolves otherwise. Other issues contained in the court's decision that are not in relation to the acceptance or rejection of the insolvency petition may be subject to appeal for reversal before the same court that passed the decision appealed.

Besides, there are other types of court order that can arise during the course of insolvency proceedings and that are not related to the acceptance or rejection of the insolvency petition. For non-final court decisions and orders, an appeal for reversal without suspensory effect can be lodged before the same court that passed the decision appealed. For judgments and final rulings, the remedy of appeal can be lodged before a second instance court.

There is no requirement for the appellant to obtain permission to appeal.

However, the right of appeal against final court rulings is subject to the payment of certain fees.

If the court's decision regarding an insolvency proceeding is appealed, a fixed amount of €800 must be paid. Further the appellant must pay 0.5 per cent of the amount of the proceeding in cases regarding claims up to €1 million, and for cases exceeding €1 million the appellant shall be charged 0.25 per cent of the claim amount, with a maximum limit of €10,000.

### Claims

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

Creditors' claims must be filed within one month after the publication of the insolvency declaration in the official gazette. If they are excluded from the creditors' list, or their claims are not fully recognised, they have the opportunity to file a claim with the court to obtain recognition of their credit claim. An appeal is available in certain circumstances before the relevant provincial court.

Generally, creditors that have prior to the insolvency declaration acquired a debt that is due and payable cannot initiate insolvency proceedings until six months have elapsed following the acquisition.

Pursuant to recent amendments of the Insolvency Act, creditors acquiring claims against the insolvent debtor after its formal declaration of insolvency shall now be entitled to vote at the creditors' meetings, unless they qualify as a related party to the insolvent debtor.

Finally, creditors who acquired a debt at a discount are allowed to file their claim for the full face value of the credit. Accrual of interest is suspended as of the date of the declaration of the insolvency except for those credits secured with rights in rem up to the maximum covered by the security.

### Modifying creditors' rights

**32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

The Insolvency Act provides that certain claims are subordinated *if, inter alia*:

- the creditor fails to comply with the obligation arising from contracts with reciprocal obligations pending at the time of the insolvency declaration, subject to certain conditions;
- the creditor is related to the debtor (ie, family members, directors and shadow directors, shareholders and companies belonging to the same group or to a shareholder holding at least 5 per cent (if the insolvent company has listed shares or debt) or at least 10 per cent (if not) of the share capital of the insolvent company); or
- the claims arise from a transaction that has been rescinded by the court where the court understands that the creditors acted in bad faith. For more information on the rescission regime please see question 39.

### Priority claims

**33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

The insolvency debts are classified as follows (see also question 38):

- debts of the insolvency estate: these include, among others, debts originating within the insolvency proceedings (eg, judicial expenses, loan agreements that are 'restored by the court), debts originating after the insolvency declaration (eg, debts arising from the continuation of the business) and salary claims for the 30 days immediately preceding the declaration of insolvency. Additionally Law 17/2014 provided that all new money granted pursuant to a collective, individual or judicially sanctioned refinancing agreement entered into on or before 2 October 2016 shall, for a period of two years from the granting of such new money, be treated as a debt of the insolvency estate. Once that period has elapsed, only

50 per cent of the new money granted will be classified as a debt of the insolvency estate and the other 50 per cent of the new money shall be classified as generally privileged debt; and

- insolvency debts: these debts are classified into:
  - specially privileged debts (among others, debts secured with mortgage or pledges, rental payments arising from lease agreements and instalments arising from hire-purchase agreements);
  - generally privileged debts (among others, salaries and severance payments up to certain limits, certain taxes, credits arising from tort liability and 50 per cent of the debt of the creditor who applied for the insolvency);
  - ordinary debts; and
  - subordinated debts, including, among others, debts owed to parties related to the debtor (see question 32).

Debts of the insolvency estate will be paid out of the debtor's assets (other than those assets attached to the specially privileged debts) with preference to any other debts. Secured debts are generally paid with the proceeds resulting from the enforcement of the security. If the secured creditor has not been entirely satisfied from the security enforcement proceeds, he will be considered an ordinary creditor for the remaining unpaid amount.

### Employment-related liabilities in restructurings

**34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

It is very common that, as a result of an insolvency proceeding, a company will start to make redundancies. Termination-related disputes would be dealt by the insolvency court rather than by the employment courts.

Depending on the number of employees affected by the termination, this will be dealt with through individual dismissal or through a collective redundancy. A termination is characterised as a collective redundancy if the redundancy applies to at least the number of employees within the following thresholds:

- 10 employees in a company with fewer than 100 employees;
- 10 per cent of the employees in a company with 100 to 300 employees;
- 30 employees in a company with more than 300 employees; or
- the redundancy involves the termination of the employment contracts of all the staff, because of the closing down of the company's activities, provided that there are more than five employees.

Apart from termination procedures, employees may initiate claims in order to request payment of unpaid salaries.

### Pension claims

**35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Pension-related claims will be considered as ordinary claims given that they fall outside of what is considered salary under Spanish law. Any pension-related disputes will be dealt with by the insolvency court.

### Environmental problems and liabilities

**36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

The Insolvency Act does not set out particular rules as regards liability arising in connection with environmental problems. Therefore, the responsibility for controlling the environmental problem will lie with the company's directors or its insolvency receiver, depending on who is in charge of managing the company. For more information on directors' duties after the insolvency declaration please see question 14.

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**Liabilities that survive insolvency proceedings**


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**37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

Privileged creditors will not be bound by the terms of a settlement agreement unless they have approved it (ie, the vote will have the effect of qualifying that creditor's claim and privilege in the manner provided for in the settlement proposal) or unless the required majority of creditors of the same class voted in favour of the settlement agreement, as set out in question 23. Therefore, the privileged creditors will be able to enforce their credits against the debtor in accordance with their own terms at the times provided for in the Insolvency Act.

The settlement agreement may also include proposals for the sale of certain assets or business units (but may not consist of a winding up of the company) where the purchaser is subrogated in full in the related debtor's obligations. See question 18.

Additionally the court may decide, upon the receivers' request, to sell an asset that is subject to security with the attached security. In this case, the purchaser is subrogated in full in the debtor's obligation, which will cease to be a debt within the debtor's insolvency proceeding.

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**Distributions**


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**38 How and when are distributions made to creditors in liquidations and reorganisations?**

The Insolvency Act provides the following rules on the payment of debts when the proceedings end with the liquidation of the debtor's assets:

- debts of the insolvency estate will be paid upon their respective maturity dates out of the debtor's assets (other than those assets attached to the specially privileged debts) with preference to any other debts;
- secured debts are generally paid out of the proceeds resulting from the enforcement of the security. If the secured creditor is not entirely satisfied from the security enforcement proceeds, he is considered as an ordinary creditor for the remaining unpaid amount;
- generally, privileged debts will be paid by segregating from the debtor's estate those assets covering the aggregate amount of such credits. The Insolvency Act lists the generally privileged debts. Each category will have priority over those below it. Within the same category, payments are made on a pro rata basis;
- ordinary debts will generally be paid on a pro rata basis after the debts of the insolvency estate, the specially privileged debts and the generally privileged debts have been satisfied; and
- subordinated debts will be paid once the remaining debts have been satisfied in full. Again, the Insolvency Act lists the subordinated debts. Each category will have priority over those below it. Within the same category, payments are made on a pro rata basis.

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**Transactions that may be annulled**


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**39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Rescission is a remedy that allows the insolvency receiver (or the creditors, in the absence of action by the insolvency receiver) to rescind acts and contracts entered into by the debtor in the two years before the insolvency declaration based on the fact that these acts or contracts are harmful to the insolvency estate.

The decision of whether a certain act or contract is harmful to the insolvency estate is to be assessed by the insolvency court in view of the pleadings and evidence put forward by the claimant. Having said that:

- certain acts and contracts are presumed by law to be harmful to the insolvency estate, without any possibility for the parties to file evidence against this presumption. This is the case for gifts and prepayments of unmatured and unsecured debt;
- the Insolvency Act also presumes (although this presumption is rebuttable), that certain acts or contracts damage the insolvency estate. This is the case of the creation of security in favour of pre-existing obligations disposals in favour of related parties (see question 32), or prepayments of unmatured secured debt;
- in the remaining cases, the claimant will have to put forward the arguments and evidence that the alleged act or contracts damages the insolvency estate; and

- transactions made within the ordinary course of business cannot be rescinded on the basis of being harmful to the insolvency estate.

The above remedy is without prejudice to the possibility to rescind those acts and contracts that the debtor had entered into in the four previous years in fraud of creditors.

If the court declares a transaction rescinded, the parties' reciprocal obligations must be restored, and the credit rights of the relevant creditor (if any) will be classified as a debt of the insolvency estate. This principle does not apply where the court understands that the counterparty acted in bad faith, in which case its claim shall be classified as a subordinated debt.

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**Proceedings to annul transactions**


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**40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

Yes. In general, the suspect period is two years prior to the insolvency declaration and four years in the case of fraud (see question 39).

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**Directors and officers**


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**41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

Directors and de facto directors (which, under Spanish law, include the concept of shadow directors), and general managers are liable to the company, the shareholders, the company's creditors and in some instances third parties, for harm caused as a result of actions or omissions that are contrary to the law or to the by-laws or that are in breach of the duties inherent to their position. Pursuant to the amendments introduced by Law 17/2014, creditors who have entered into the refinancing agreement described in question 39 will not be considered de facto directors by reason only of the obligations assumed by the debtor as a consequence of the viability plan within the framework of the refinancing agreement.

Spanish corporate law specifically provides for two types of actions for breach of a directors' duty:

- a corporate action that aims to protect and recover the company's assets damaged by the actions of the directors; and
- an individual action that aims to protect and recover the personal assets of the claimant to the extent damaged by the actions of the directors.

Additionally, directors can be held jointly and severally liable with the company for the company's debts if the company ceases to comply with certain subscribed capital-to-equity ratios and such ratios are not re-established, in which case the directors are under the legal duty to procure the liquidation of the company. In such circumstances, the liability of directors would be for the debts borne after the breach of the capital-to-equity ratio.

Furthermore, the insolvency court may declare the director liable for any damage during the qualification phase of the insolvency (ie, the phase that aims to investigate the potential liability of third parties) if the insolvency is classified as 'guilty'. An insolvency would be deemed 'guilty' when, in the creation or worsening of the state of insolvency there was wilful misconduct or gross negligence by the company or, among others, its directors. The judicial decision may order:

- disqualification of the directors from managing third-party assets or representing or managing any person or company for between two and 15 years;
- removal of the directors' rights as creditors of the debtor;
- return of the directors' rights or assets that have been unduly obtained from the debtor;
- payment of indemnities for any loss or damage caused; and
- (in certain circumstances) that the directors are liable for the deficit to creditors.

Finally, the Criminal Code includes a number of criminal offences that may apply to a director, for instance, when falsifying the annual accounts in such a way to cause financial damage to the company, to any of its shareholders or to a third party, with this offence being punished with imprisonment from one to three years and a fine from six to 12 months.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

In the framework of an insolvency proceeding classified as 'guilty', the parent company would be liable if the parent had given instructions to the insolvent company that caused or exacerbated the insolvency. In such a case, the parent company's directors could be deemed de facto directors (ie, persons who, without being formally appointed as directors, are acting as such) of the insolvent company who, as such, could ultimately be responsible for indemnifying third parties for any loss or damage caused by the insolvent company. Furthermore, if the insolvency proceeding ends with the liquidation of the company, the court may also rule that the de facto directors pay any outstanding amounts upon liquidation to the company's creditors.

Separately, if a refinancing agreement is frustrated because the debtor rejects, without a reasonable cause, the terms of a debt-for-equity swap transaction that complies with certain requirements, the shareholders (and directors) of the debtor may face personal liability in the event of any future insolvency.

The Insolvency Act only envisages that the insolvency of companies belonging to the same group are heard before the same judge, but the different proceedings are not unified or amalgamated. Therefore, each insolvency proceeding follows its own separate regime, with the relevant insolvency estates remaining separate. The judge in charge of the proceedings shall seek good coordination of the different proceedings.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Yes, 'related party' claims rank as subordinated, with the consequence that these debts will only be repaid once the remaining debts have been satisfied in full (for more information on the ranking of the credits, please see question 38).

If the insolvent debtor is a natural person the following will be considered a 'related party':

- the spouse of the insolvent debtor or a person who has been such during the two years prior to the insolvency declaration, or individuals who cohabit with a similar relation of affection or who have done so during the two years prior to the insolvency declaration;
- the ascendants, descendants and siblings of the insolvent debtor or of any of the aforementioned persons;
- the spouses of the ascendants, descendants and siblings of the insolvent debtor;
- legal entities controlled by the shareholder or his or her relatives and the de iure or de facto directors of such legal entities;
- legal entities forming part of the same group of companies as those mentioned above; and
- legal entities in respect of which the individuals or legal entities mentioned above qualify as de iure or de facto directors.

If the insolvent debtor is a company, the following will be considered a 'related party':

- shareholders and if they are natural persons, the related parties set out above, who are, pursuant to the law, personal and shareholders of an unlimited company;
- the insolvent company's directors and de facto directors, the insolvent company's liquidators and the attorneys with general powers to run the insolvent company, as well as those who have acted as such during the two years prior to the insolvency declaration;
- shareholders that, when the relevant debt arose, directly or indirectly owned at least 10 per cent of the shares of the insolvent company, except when the insolvent company is a listed company or a company with listed debt when this level is 5 per cent; and

- companies in the same group as the insolvent company and their common shareholders, provided that they meet the requirements set out in the immediately preceding point.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Seizure of the debtor's assets can only take place by obtaining a court order. Initiation of insolvency proceedings automatically triggers a moratorium on the seizure of the debtor's assets (see question 15).

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

All commercial entities may be liquidated for any of the following reasons:

- expiry of the term fixed by the shareholders or partners in the by-laws;
- completion of the corporate purpose for which the commercial entity was set up; or
- loss of capital.

As previously mentioned, most Spanish companies are either corporations or limited liability companies. These companies may be liquidated in the following circumstances:

- if it is no longer possible to accomplish the purpose for which the company was incorporated or, as a result of the paralysis of the management bodies of the company its continued operation becomes impossible;
- the losses have reduced the equity to an amount below 50 per cent of its share capital, unless the share capital is restored to the necessary amount;
- if the share capital is reduced to below the legal minimum amount;
- if there is a merger or split of the company; or
- for any other cause established in the by-laws.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Insolvency proceedings are always concluded by an order issued by the relevant court in the following circumstances:

- an appeal against the insolvency order is successful;
- the debtor has fully complied with the court-approved settlement;
- all claims have been paid or creditors have been fully satisfied;
- if there is evidence that there are no available assets to pay the creditors; and
- if all creditors waive the outstanding claim.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

The EU Regulation on Insolvency Proceedings applies in Spain (see the chapter on the European Union). Regulation (EU) 2015/848 of the European Parliament and of the Council on insolvency proceedings (the Recast Regulation) will apply to insolvency proceedings from 26 June 2017. This new regulation updates European Union rules on cross-border insolvency procedures with respect to the currently applicable Regulation 1346/2000.

In addition, the recognition of non-EU insolvency proceedings is available in Spain through the exequatur proceedings contained in the

Civil Procedure Act, provided that the following requirements set out in the Insolvency Act are met:

- the foreign decision refers to collective proceedings grounded in the insolvency of a debtor by virtue of which all of its assets and activities are controlled or supervised by a tribunal or authority in relation to its liquidation or reorganisation;
- the foreign decision is final;
- the competence of the foreign court is based on the jurisdictional criteria provided by the Insolvency Act (ie, centre of main interests or domicile) or there is a reasonable connection equivalent to the aforementioned criteria;
- the decision has not been rendered in the absence of the debtor, or it has not been rendered after the summoning of the debtor in due form and with sufficient time for it to properly defend itself; and
- the decision is not against public policy.

Foreign insolvency proceedings will be recognised as main insolvency proceedings (if foreign insolvency proceedings are opened in a country where the debtor has its centre of main interests) or as a territorial foreign proceedings (if foreign proceedings are opened in a country where the debtor only has an establishment or assets devoted to a certain business activity). The UNCITRAL Model Law was taken into consideration by the drafters of the international conflict rules contained in the Insolvency Act, however, Spain has not formally adopted the UNCITRAL Model Law.

## COMI

### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

In case of a legal person the Insolvency Act establishes that the place of the registered office shall be presumed to be the COMI. To this effect, a change of registered office carried out in the six months prior to the insolvency declaration is ineffective. The Recast Regulation (Regulation (EU) 2015/848) applicable to insolvency proceedings from 26 June 2017 establishes that the presumption that a debtor's COMI is in the place of the registered office will not apply if the COMI has shifted in the preceding three months. For more information on the COMI regulation under the EU Regulation and the Recast Regulation, see the chapter on the European Union.

Spanish courts have had the chance to examine the COMI of companies on several occasions, in which they have mainly analysed the location in which the management decisions are taken. In general, factors that have been held to be relevant to determine a debtor's COMI (in addition to the rebuttable registered office presumption) are: location of internal accounting functions and treasury management, governing law of main contracts and location of business relations with clients, location of lenders and location of restructuring negotiations with creditors, location of human resources functions and employees

as well as location of purchasing and contract pricing and strategic business control, location of IT systems, domicile of directors, location of board meetings and general supervision. Spanish courts have in the past tended to focus on the location of the principal business operations and the location of assets.

As regards a corporate group of companies, in Spain there is no specific test to determine the COMI. Hence, in general, the parent company and each subsidiary of a corporate group is subject to an individual and entirely separate insolvency proceeding (but see question 29 on the insolvency of corporate groups). See the chapter on the European Union for new EU Regulation on group insolvencies.

## Cross-border cooperation

### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

Recognition in Spain of EU insolvency proceedings is available through EU Regulation 1346/2000 and the Recast Regulation (Regulation (EU) 2015/848), with this recognition being automatic. For more information on recognition of foreign insolvency proceedings, please see the chapter on the European Union.

In addition, the EU Regulation 1346/2000 on cross-border insolvency proceedings, the Recast Regulation and the Insolvency Act (which contains similar rules to those contained in the EU Regulation for non-EU insolvency proceedings) establish the duty of reciprocal cooperation for domestic and foreign administrators. Cooperation is basically focused on exchange of information, coordination of the administration of assets and the possibility of enacting concrete cooperation rules.

We are not aware of any case where Spanish courts have refused to recognise foreign proceedings or to cooperate with foreign courts.

## Cross-border insolvency protocols and joint court hearings

### 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

The international rules contained in the Insolvency Act contain specific provisions on the coordination of parallel insolvency proceedings, including duties of cooperation on insolvency receivers (by exchange of information, coordination of administration and supervision and the possibility for the Spanish courts or authorities to render rules on the coordination of proceedings). We are not aware of any public protocols or agreements reached between courts or authorities.



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# Sweden

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

Under Swedish law, there is a difference between liquidation of an insolvent company and liquidation according to the Swedish Companies Act (2005:551). When liquidation (bankruptcy) is used here, it is only meant to refer to the liquidation of an insolvent company according to the Swedish insolvency regime as described below.

Swedish insolvency law is mainly regulated in the Bankruptcy Act (1987:672) and the Reorganisation of Business Act (1996:764) but rules regarding the event of insolvency are also found in many other legal areas, such as for example within the company law, the employment law and the property law.

The basic provisions on bankruptcy (where the insolvent business is wound up) are found in the Bankruptcy Act. This Act governs petitions and declarations of bankruptcy, effects of bankruptcy, recovery, claims in bankruptcy, duties of the debtor, administration of the bankruptcy estate and supervision of the bankruptcy.

Statutory provisions regarding reorganisation are to be found in the Reorganisation of Business Act. This contains provisions governing how a debtor with financial difficulties can reorganise its activities with the protection of the court, which prohibits enforced collection and execution of debts arising prior to that date. There are also provisions on the appointment of an administrator to safeguard the creditors' interests, the administrator's duties, the obligations of the debtor, the reorganisation plan and the creditors.

The Reorganisation of Business Act also contains detailed provisions regarding public (compulsory) composition, which may take place against the wishes of the creditors and which takes the form of a public composition proceeding.

Several laws apply in tandem with the Bankruptcy Act and the Reorganisation of Business Act. These include:

- the Rights of Priority Act (1970:979), which governs the priority of claims between creditors; and
- the Salary Guarantee Act (1992:497), which ensures that the employees of a bankrupt company receive their salaries.

In Sweden a debtor is considered insolvent when it is unable to pay its debts as they fall due, and this inability is not only temporary. A petition for bankruptcy may be filed with the court by the debtor. In these cases, the company is normally declared bankrupt on the same day as the petition was filed.

A petition for bankruptcy may also be filed by a creditor, who is then, according to the Bankruptcy Act, required to prove that the debtor is insolvent, for example by showing the following:

- an attempt by the Swedish Enforcement Authority to enforce a writ of execution (a writ of execution may be attained (if not disputed) through summary proceedings at the Enforcement Authority or through normal court proceedings) has been carried out during the past six months, revealing that the debtor did not have enough assets to cover the claim;
- the debtor, who is, or within one year prior to the bankruptcy petition has been, liable to keep accounts under the Accounting Act has failed to pay an undisputed and due debt within one week of a

demand for payment being made by the creditor and the creditor has filed for bankruptcy within the following three weeks; or

- the debtor has suspended payments and has informed a substantial number of creditors of such suspension.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The court of first instance in both bankruptcy and reorganisation proceedings is the district court, whose decisions may be appealed to the court of appeal and ultimately the Supreme Court.

Generally speaking, in bankruptcies the court's jurisdiction is confined to appointing a trustee in bankruptcy and determining the right of the creditors to receive payment after it has decided that proofs of debt in the bankruptcy are to be filed and whether to approve the trustee's dividend proposal. Separate proceedings must be instituted in respect of disputes and claims for priority regarding property and the collection of outstanding debts in accordance with general principles of judicial procedure.

The district court has no direct jurisdiction over the assets of the debtor. These are administered independently by the trustee, albeit subject to a duty in certain cases to consult with the creditors holding security in the property.

In business reorganisations the district court appoints an administrator and also administers public composition proceedings upon request from the administrator.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

No legal entities are excluded from insolvency proceedings. Special regulations do apply to some legal entities, such as certain banks.

According to the main rule, the assets available to creditors under both bankruptcy and public business reorganisation proceedings are the assets that belonged to the debtor at the time the court opened the relevant proceedings together with any assets that accrue during the relevant proceedings. The assets are normally not available to meet individual claims; however, if the debtor's assets have been attached to meet specific claims before the insolvency proceedings were commenced, enforcement will normally take place against those assets, notwithstanding the proceedings.

There are a number of exceptions to the main rule as stated above:

- Where an order for attachment is obtained prior to the opening of the bankruptcy proceedings and the party that obtained an order for attachment did not have a legal charge against the asset to which the order for attachment applies and the priority right that was attained by the attachment is annulled, either by agreement or by the court, the trustee may, up until the assets have been sold, request that the order for attachment shall also be annulled.
- Property belonging to the bankruptcy estate to which a legal charge for a certain claim applies may be attached to the claim despite the opening of bankruptcy proceedings.

- If there is litigation pending between the debtor and a third party regarding title to a particular asset and the debtor chooses not to pursue the action, the asset will not be available to the creditors.
- The Bankruptcy Act provides protection to a third party who enters into transactions with the debtor up to the day after the public notice of the opening of bankruptcy proceedings was published in the official gazette. If the debtor enters into a transaction during this period and the third party was unaware of the opening of bankruptcy proceedings, the transaction will be binding on the debtor. The debtor may also unwind the transaction by repaying the third party.
- Assets belonging to third parties that have been rented or leased by the debtor are generally not included in the bankruptcy estate. However, there is a rebuttable presumption that assets that are in the debtor's possession at the time that the bankruptcy proceedings are commenced are part of the bankruptcy estate, unless parties are able to prove the existence of their rights over the assets in question. In order to prove ownership in relation to intangible assets or assets of fungible nature, a third party claiming the assets would have to establish that the debtor was required to keep the assets in question separate from its other assets.
- Money that at the time of the opening of the bankruptcy proceedings was held by the debtor on trust for a third party does not belong to the bankruptcy estate. However, to establish a right of reclamation to such assets, the third party would have to establish that the provisions of the Funds Accounting Act have been complied with, including that the money in question has been kept separate from the debtor's other assets prior to the bankruptcy.
- If a third party has purchased goods from the debtor, but the goods have not yet been delivered, the third party may still be entitled to the goods if it has been registered as the owner in accordance with the provisions in the Act of Trade with Goods that the Purchaser Leaves in the Seller's Possession. In relation to moveable property, the legislation allows the purchasers to register their interests in the property in question; however, the procedure is not commonly used.
- A supplier who, before the opening of bankruptcy proceedings, has delivered goods to the debtor, in compliance with the terms of retention of title, may be entitled to claim those goods back if the debtor has not paid for the goods. Retention of title is common with regard to machinery, motor vehicles and other equipment of significant value that is intended to be used for a considerable time by the purchaser. It is not available in respect of goods that are intended for resale by the purchaser.
- Under the provisions of the Commission Agency Act, a commission agent may undertake to sell goods on behalf of another party but in the name of the agent. If the debtor acts in this capacity, the principal may be able to recover the goods following bankruptcy proceedings being opened in respect of the agent as title will be held by the principal until the moment of resale.
- If the debtor is an individual some assets are excluded from insolvency proceedings with respect to the debtor's needs, such as necessary clothes, furniture, work tools, an apartment that is considered a permanent home, etc. Some assets are also excluded with respect to the nature or purpose of the assets, such as assets received through a gift or will, money received with a charitable purpose from, for example the state, a community or a foundation or rights to pension benefits.

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### Public enterprises

#### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The Swedish government, municipalities and authorities cannot be declared bankrupt in Sweden.

As regards all other enterprises, the same rules apply, regardless of whether the bankrupt enterprise is partially or wholly government-owned.

If a financial institution goes bankrupt, a state-provided guarantee covers deposits in banks and some other financial institutions. According to the Swedish Deposit Insurance Act (1995:1571), the insurance provides compensation up to €100,000 per customer (including distribution from the bankruptcy).

Unlike the rules in the Bankruptcy Act, the Reorganisation of Business Act does not apply to banks or other financial institutions or enterprises where the Swedish government or municipalities exercise a controlling influence.

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### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

In February 2016, Sweden implemented, through a regulation, the European Recovery and Resolution Directive (59/2014), which introduces a framework for resolution of credit institutions, investment firms and companies in the same group as such companies.

One of the main features in the resolution process is that the company's owners and lenders, rather than the state, will bear any losses in the company. The regulation aims not only to provide opportunities to reorganise or liquidate the above-mentioned companies, but also to avoid individual companies ending up with problems that may lead to a resolution. The regulation includes provisions concerning resolution, the preparations of such procedures and preventive supervisory measures.

The recovery and resolution regulation grants the Riksgälden (the resolution authority) the power to impose extensive measures, which are to be applied in accordance with the circumstances in each individual case. One of these measures is to write down the bank's debt, starting with debt that would be considered unsecured in an ordinary bankruptcy.

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### Secured lending and credit (immoveables)

#### 6 What principal types of security are taken on immoveable (real) property?

Security interest in real property, ships and aircraft is created by mortgaging. Upon the registered owner's applications, such mortgages are registered at the relevant registration authority and certified by a deed of mortgage (mortgage certificate), which is handed to the owner. The owner can pledge these deeds to creditors according to the rules of ordinary chattels (ie, it must hand the deed over to the pledgee (mortgagee)). The deed holder is protected by possession of the document alone. The deed is normally 'handed over' electronically nowadays.

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### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

Chattels can be pledged by an oral or written agreement but have to be handed over to the pledgee. The monies that originate from the pledge must be paid to the pledgee to a secured account. The chattels must remain in the possession of the pledgee and the pledgor must not be allowed to independently have the use of them. Chattels that are in the possession of a third party may be pledged by their owners. In such a situation, the transfer of the goods is replaced by notification from the pledgor or the third party.

The pledge only secures the individualised pecuniary claim for which the goods have been pledged. It is uncertain under Swedish law whether it is possible to pledge goodwill or intangible property. Patents and trademarks, as well as applications to register patents and trademarks, can be pledged. The security interest is authorised by filing a written agreement to pledge the property with the registration authority. In cases where it is impossible to hand over the asset, the transfer can often be replaced by notification.

Under Swedish law, security assignments (which, in fact, are very similar to pledges) of individual moveable items of property are accepted. The purchaser will, however, not be protected against third parties until it has taken possession of the goods (or sometimes by notification), or their possession has been registered in accordance with a special procedure.

Under Swedish law, it is also possible to give a security interest known as a floating charge over the changing assets of a business enterprise. The owner of the property obtains a floating charge deed (certificate) by virtue of registration in a central register. To grant the security, the debtor must pledge the floating charge deed and transfer the deed to the creditor. The value of the floating charge is 100 per cent of the moveable assets (not encumbered by pledges or otherwise) with some

exceptions such as shares, cash and bank deposits. In this context, it can also be noted that leasing and factoring is more commonly used instead of the above-mentioned traditional security devices.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

Non-preferential creditors are only able to obtain payment by seizure or bankruptcy proceedings. In order for them to receive payment by means of seizure, the creditor must obtain a writ of execution. No writ of execution is needed to obtain payment in bankruptcy.

A writ of execution can be obtained through a summary payment procedure within a few months, unless the debtor contests payment and the case is remitted to a general court of law.

In light of the present case load facing the courts, it may be a year before a judgment is obtained in one of the lower courts. If a possible appeal by the losing party is taken into account, there may be a delay of another year before the case is finally decided.

The claims of foreign creditors are treated no differently from the claims of Swedish creditors.

The concept of pre-judgment is not used.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

The board of directors or a general meeting of shareholders of an insolvent corporation may pass a resolution to file a petition for bankruptcy. If the petition, signed by authorised persons, is presented to the court, the company will immediately be declared bankrupt and the liquidation process is opened. When a debtor has been declared bankrupt, the district court must appoint one or more trustees in the bankruptcy as soon as possible. This appointment is valid for the whole bankruptcy proceedings.

A bankruptcy estate comprises all property belonging to the debtor at the time it was declared bankrupt or accruing to it during the proceedings, and which is capable of being seized.

When the debtor has been declared bankrupt, the trustee assumes full authority over the debtor's property. The trustee may, if he or she considers it appropriate, allow a bankrupt enterprise to continue trading for up to one year and two months from the declaration of bankruptcy, or longer if there are particular reasons for doing so.

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

The main rule is that any claim entitles a creditor to file a petition for bankruptcy regarding an insolvent debtor. The creditor is under a duty to prove its claim.

The creditor bears the burden of proving that the debtor is insolvent but may prove the fact in any way whatsoever (see question 1). In certain cases there are statutory rules as to a presumption of insolvency.

The effects of the start of an involuntary liquidation are the same for a voluntary liquidation (see question 9).

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### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

The board of directors of a corporation with financial difficulties may pass a resolution to file an application for the start of business reorganisation proceedings according to the Reorganisation of Business Act.

Upon such an application, the court will open a business reorganisation and appoint an administrator for the purposes of examining the debtor's affairs and negotiating the reorganisation with the creditors. The court will not decide to open the reorganisation if there is no good reason to suppose that a reorganisation will succeed. The debtor need not provide proof of insolvency in its application, only proof that shows its difficulties in paying debts and a reasonable possibility of achieving the proposed reorganisation.

Business reorganisation proceedings are begun by a district court's opening order and the appointment of the administrator.

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### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

The court will only approve a creditor's application for reorganisation if the debtor agrees to it.

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

There is no formal requirement to apply for bankruptcy within a certain time period. However, the directors of an insolvent limited liability company (and even some directors) may risk personal liability as well as criminal charges if they continue the company's operations and by that incur damage to a creditor or another. For instance, the directors may be personally liable for a creditor's damage claims if the company has entered into an agreement knowing that it is insolvent and unable to fulfil the agreement.

Also, as a means to protect the creditors of a Swedish limited liability company, the Swedish Companies Act provides that a limited liability company may be forced to wind up if it is suffering from a financial crisis. The mandatory rules in the Swedish Companies Act stipulate that a limited liability company may be forced to wind up if the shareholder's equity is less than half of the registered share capital. Should the board members of the company fail to fulfil their duties under these provisions, they are jointly and severally liable for those of the company's obligations that subsequently accrue.

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

The Reorganisation of Business Act does not regulate the ways in which the debtor's property may be used or sold. The debtor retains control over its property but must consult the administrator, whose duty it is to ensure the best interests of the creditors. If the debtor neglects his duties in this respect, the court can bring the proceedings to a halt. Ultimately, the potential for sale is regulated by the provisions regarding recovery in the Bankruptcy Act.

The business of the debtor must be conducted in such a way that its overall financial status does not deteriorate and no creditors' positions are altered in relation to others. As a matter of principle, old non-preferential claims may not be paid unless the creditor in question can be considered of particular importance for a successful reorganisation.

To facilitate the reorganisation, the debtor, with the consent of the administrator, is allowed to raise new loans, which will be preferential in a bankruptcy (liquidation) situation. This is also applicable in business reorganisations on claims based on agreements entered into by the debtor during the reorganisation, provided that the administrator consented to the agreements being entered into.

To prevent suppliers and others from undermining the entire reorganisation by cancelling contracts because of the debtor's difficulties in paying its debts, special rules have been created for contractual relationships. These rules give the debtor the opportunity, with the consent of the administrator, to demand fulfilment on both sides. Under certain conditions, the other party is entitled to some sort of security.

As a rule, when the administrator has been appointed he should contact the creditors with a notice of the start of the proceedings, for an exchange of information and to see whether the business reorganisation proposal is acceptable.

If required by any creditor, the court appoints a creditors' committee consisting of three creditors at the most. The administrator has an obligation to consult with the committee, unless it is impossible because of lack of time or similar reasons.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

The general rule is that a creditor's pecuniary claim should be filed and tested in the bankruptcy proceedings. It is possible for a creditor who has started legal proceedings before the declaration of bankruptcy to continue the proceedings, although it is likely that a court decision in such a case has to be tested again in the bankruptcy proceedings.

Should legal proceedings regarding ownership of assets be pending at the time when the debtor is declared bankrupt, the proceedings will most likely continue and the bankruptcy trustee has a right to assume the debtor's position in the proceedings.

When the debtor has been declared bankrupt, only a creditor holding a pledge (including mortgages) is allowed to continue execution procedures (through the Enforcement Authority). Sales of pledged assets other than through the Enforcement Authority are restricted in several ways and may need the consent of the trustee. Property that is not pledged or mortgaged, including assets to which a creditor has a security interest by way of a floating charge, is sold by the trustee.

With regard to business reorganisation, the opening of such proceedings does not stay legal proceedings as such. The opening of a business reorganisation is intended, among other things, to prevent independent actions on the part of one or more of the creditors. For this reason, a petition for bankruptcy filed by a creditor after the start of a case is to be declared suspended. Only if there are reasons to believe that the debtor is acting in a way that endangers the rights of the creditor may he be declared bankrupt during a business reorganisation. Furthermore, as a general rule, the proceedings stay any execution proceedings if the creditor is not secured by a pledge. Sequestration is also not allowed.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

When the debtor has been declared bankrupt, the trustee assumes full authority over the debtor's property. The trustee may, if he considers it appropriate, allow a bankrupt enterprise to continue trading for up to 14 months from the declaration of bankruptcy, or longer if there are particular reasons for allowing so. Loans or credit obtained during the continuance of trading are treated as debts of the bankruptcy estate and must be paid before any other debt.

In a business reorganisation, the debtor remains in full control over its property and the continuing business but must consult the administrator. The business of the debtor must be conducted in such a way that its overall financial status does not deteriorate and so that no creditor's position is altered in relation to other creditors. To facilitate the reorganisation, the debtor, with the consent of the administrator, is allowed to raise new loans, which will be preferential in a bankruptcy situation.

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### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

A claim made against the debtor in bankruptcy may, as a rule, be set off by a creditor against a claim that the debtor had against him when he was declared bankrupt. This does not apply if, owing to the nature of the claim, such claim could not have been possible to set off if there had been no bankruptcy or if the counterclaim was acquired during the period starting three months before the debtor was declared bankrupt.

Also, in a reorganisation, counterclaims may be set off by a creditor against debts owed to the debtor. Generally speaking, counterclaims acquired during the three-month period before an application

for the opening of a business reorganisation is filed may not, however, be offset.

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### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

(See question 14.) The general Swedish law rules apply to the sale of assets and, accordingly, adherent liabilities can pass with the assets. In a bankruptcy, the estate will generally strive to sell the assets 'free and clear'. The sale procedure can be arranged to allow for stalking horse bids and, subject to the buyer having security in the asset or having a priority claim, it is generally possible to credit bid in sales of an insolvent debtor, although it is, perhaps, not that common. In Sweden, the court is not involved in a sale of assets, instead the bankruptcy trustee is in charge of the process.

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### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

Swedish law in this area does not expressly regulate the situation and Swedish case law does not present any firm answers to the issues at hand.

If a debtor has entered into an agreement including IP rights, a trustee, generally speaking, should have the right to assume the obligations of the agreement and use the IP rights. This is on the condition that the estate can fulfil the conditions of the agreement. A termination by the licensor or owner of the IP right can be possible because of the long duration of many IP agreements and because the IP agreement may be incompatible with the liquidation of the entity in a bankruptcy. This is especially so, as it is often not possible to transfer the IP right; thus it is generally not possible for a new licensee to fulfil the obligations under the agreement. The estate of a licensee has no right to terminate the licence agreement while at the same time utilising the IP rights.

Whether a licensee of IP rights is protected in a bankruptcy of a licensor is uncertain. This protection is, however, somewhat limited and does not include fulfilment of obligations such as support, education, the provision of know-how, etc, unless the trustee decides to assign the agreement in full.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

As long as the purchaser's purpose with the processing of customer data is the same as the purpose of the insolvent company, then a transfer of customer data is permitted. However, to be able to preserve its right, the customer must be informed of the identity of the new data controller. If the purchaser intends to use the customer data for any other purpose than the insolvent company's, then a new data processing is at hand that will require legal ground (consent/statutory justification, etc) in the Swedish Data Protection Act.

If customer data are used in the insolvency process, the insolvency administrator does not need the individual's consent to process the data for the purpose of drafting a bankruptcy estate inventory and similar measures obliged in an insolvency process. However, if the insolvency administrator publishes personal data online, for example, by uploading the bankruptcy estate inventory, then the individual's consent may be required to do so, depending on the kind of information that is published.

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**Rejection and disclaimer of contracts in reorganisations**

- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

No, a debtor cannot reject or disclaim an unfavourable contract only based on the reorganisation. The provisions of the contract, including provisions regarding breach of contract, will apply with the addition of the possibility to demand fulfilment as mentioned above (see question 14).

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**Arbitration processes in insolvency cases**

- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

It is not common to use arbitration procedures in insolvency proceedings. A bankruptcy estate is, according to a ruling by the Supreme Court, under certain conditions, bound by an arbitration clause that was agreed before the insolvency proceedings were initiated. If the dispute concerns a monetary claim in the bankruptcy, the interpretation of the Supreme Court ruling is that other creditors must also be allowed to intervene in the proceedings. Disputes regarding rights in rem and rules regarding protection of creditors in the Swedish Companies Act could be tried in other proceedings, despite an arbitration clause. The estate normally has the opportunity to agree to arbitration procedures to settle disputes.

Arbitration procedures that are initiated at the opening of the bankruptcy can normally continue and the trustee has the choice of whether to enter into arbitration procedures or not.

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**Successful reorganisations**

- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

The administrator, having consulted the debtor, should draw up a reorganisation plan specifying the actions that must be taken to resolve the business problem and send it to the court and the creditors. If it is not possible to reach an informal settlement with the creditors on the basis of the plan, the debtor can apply for a public composition proceeding to begin.

The Reorganisation of Business Act only contains provisions regulating the approval of compulsory composition proceedings, if such a procedure has been a part of the reorganisation. A meeting is called with the creditors before the court, where voting on the composition should take place, shortly after the court has ordered that public composition proceedings are to take place. The decision of the creditors is then to be approved by the court, unless there are reasons preventing such an approval.

The Reorganisation of Business Act stipulates that the public composition proposal (if applicable) must only specify how much the debtor offers to pay, when payment is to be made, whether security has been provided for the composition and if so, what it comprises.

Only non-preferential claimants participate formally in composition proceedings pursuant to the Reorganisation of Business Act. Preferential creditors are expected to receive full payment of their claims. If a creditor has security in a particular property and the value of that property does not fully cover the claim, the creditor participates in the composition in respect of the residue of its claim.

Releases of third parties are not included in a reorganisation plan.

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**Expedited reorganisations**

- 24 Do procedures exist for expedited reorganisations?**

There are no specific procedures for expedited reorganisations, however, the existing procedures (bankruptcy and reorganisation) can be used for expedient procedures in a very effective way.

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**Unsuccessful reorganisations**

- 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

As mentioned above, in a business reorganisation situation it is necessary to reach an informal settlement with the creditors. Such a settlement can only be reached if the creditors agree to concessions of their claims and do not oppose such a settlement. If an informal settlement cannot be reached, the debtor can apply for the start of public composition proceedings. If in such proceedings the creditors at the meeting before the court do not vote in favour of the proposal, the court will rule upon it and the reorganisation will end.

If the debtor neglects his or her duties, a creditor may request the court to declare the concession of that creditor's claim void. The Bankruptcy Act gives the creditors the right to file a petition for bankruptcy, should the debtor not perform according to the approved plan.

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**Insolvency processes**

- 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

The creditors in a bankruptcy are notified by the district court that the debtor has been declared bankrupt, whether or not it is anticipated that a dividend will be paid and whether or not it has been decided that proofs of debt should be filed with the court.

Only in complicated bankruptcies and where non-preferential creditors may receive a dividend do the creditors need to file proofs of debt with the court. In such cases, the creditors are notified by the court of the date by which such proofs must be filed.

The trustee alone administers the winding-up of the estate. The trustee is under a duty to safeguard the rights and interests of the creditors and to take all measures necessary to achieve a favourable and rapid winding-up. The trustee is also under an obligation to obtain the consent of creditors holding security in real property and personal property before selling such property. No formal creditors' meetings are held and no formal committees exist. Reports and the information submitted to the court is public and is available. There are different reports to be submitted to the court, such as the initial estate inventory, the trustee's report on, inter alia, the condition of the estate and the semiannual reports. In addition, the trustee has an information obligation towards, inter alia, creditors.

Should a creditor not be satisfied with the trustee's administration, it may file a request with the court for the trustee's dismissal. If the court grants such a request, a new trustee is appointed. A creditor can, on behalf of the estate, initiate recovery proceedings should the trustee decide not to do so.

In business reorganisations creditors do not receive information that an application to open a reorganisation has been submitted to the court. However, the administrator shall notify all known creditors of the decision to initiate the proceedings within one week from the court decision. In the event that the number of creditors with claims without priority is very large, notice to such creditors could be made through general publication, rather than individual notifications.

A reorganisation plan may provide for release of liabilities, however, it is not very common. Instead, the reorganisation plan is normally focused on the debtor's liabilities.

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**Enforcement of estate's rights**

- 27** If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

With regard to voidable transactions (recoveries), creditors have the right to pursue such a transaction if the trustee decides not to use his or her right. In such a case, the creditors have the right to be reimbursed for legal costs from the recovered assets, but the surplus belongs to the estate.

The creditors could either fund the estate or acquire claims (other than recoveries) if accepted by the estate. In the latter case, the fruits of the remedies belong to the creditor.

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**Creditor representation**

- 28** What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

No formal creditors' meetings are held and no formal committees are formed in a bankruptcy proceeding. There is an obligation for the trustee to consult with the creditors that are directly affected on more important issues. A creditor that is dissatisfied with the trustee's administration has the right to request the appointment of an examiner for the supervision of the trustee's administration. The creditor appointing the examiner shall bear the costs.

If requested by a creditor in a business reorganisation, the court may appoint a creditors' committee consisting of a maximum of three creditors. The committee is chosen among the creditors and will most often consist of representatives for the state, the largest lender and a supplier. The administrator has an obligation to consult with the committee, unless it is impossible because of lack of time or similar reasons.

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**Insolvency of corporate groups**

- 29** In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Insolvency proceedings involving a corporate group are not formally combined. Depending on the circumstances, however, the same person can be (and often is) appointed as the trustee for the different group of companies to save on costs and combine values. The assets and liabilities may not be formally combined into one pool. Each legal entity is treated independently and there are no Swedish rules that allow transfer of assets to an administration in another country.

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**Appeals**

- 30** What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

The court of first instance in both bankruptcy and reorganisation proceedings is the district court, whose decisions may be appealed to the court of appeal and ultimately to the Supreme Court.

All formal decisions taken by the courts are possible to appeal to the next instance. The court of appeal and the Supreme Court do, however, require a leave of appeal.

There are no requirements to post security in connection with an appeal.

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**Claims**

- 31** How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

If the trustee is able to ascertain which creditors are entitled to payment in the bankruptcy, it will not be necessary for proofs of debt to be filed. In such a case, the creditors only need to notify the trustee of their claims. However, in more complicated bankruptcies and, as a rule, in bankruptcies where non-preferential creditors receive a dividend, proofs of debt must be filed. If this is the case, known creditors will receive notification from the district court of the period in which proofs must be filed with the court. Upon payment of a small charge, creditors may file proofs of debt after such deadline has expired and until the bankruptcy is concluded.

In bankruptcies where proofs of debt do not need to be filed, objections to the trustee's dividend proposal may be made, upon which the court will consider and rule on the proposal. Where it has been decided that proofs of debt are to be filed, the court will consider the validity of a creditor's claim if the trustee or another creditor has made an objection to such a claim.

Generally, counterclaims may be set off by a creditor against debts owed to the debtor. Counterclaims acquired during a 90-day period before the application for bankruptcy has been filed may not be set off. Claims against the debtor may, with the foregoing limitation, be sold or transferred. There is no obligation to disclose transfers and claims acquired at a discount can be enforced for its full face value. It is not possible to create a set-off situation after the bankruptcy has been initiated as set-off will be tried under the circumstances as of the date of the bankruptcy.

Claims for contingent and unliquidated amounts can be recognised; however, not if there is no reason to assume that the condition will be fulfilled.

Interest accrued after the opening of an insolvency case may be claimed, but only if all debts all paid in full.

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**Modifying creditors' rights**

- 32** May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The priority order cannot be modified by the court except for recoveries (voidable transactions).

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**Priority claims**

- 33** Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

Claims against the bankruptcy estate itself (costs incurred by the estate after the debtor has been declared bankrupt) as well as the trustee's fee must always be paid before other claims.

The floating charge extends to 100 per cent of moveable assets (not encumbered by pledges or otherwise) with some exceptions such as shares, cash and bank deposits.

The priority order is generally as follows.

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**Security in certain assets**

- Maritime liens;
- aircraft liens;
- claims of pledges, repairer's liens and other rights of retention;
- claims secured by a floating charge; and
- claims secured by a mortgage in real property.

**General priority**

- Costs for a petition in bankruptcy;
- costs for the fee of the administrator in a business reorganisation;
- costs and claims relating to agreements entered into during the business reorganisation with the administrator's consent;
- auditing costs;
- (employees' salary claims); and
- unsecured creditors.

**Employment-related liabilities in restructurings****34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

Employees are normally terminated because of shortage of work in a bankruptcy, and sometimes also during a reorganisation. Such employees are entitled to all employment benefits during their individual notice period.

The wage guarantee applies to company restructurings and bankruptcies. This can create some financial support during the initial continuing business under a bankruptcy or a restructuring. The wage guarantee covers most of the prioritised salary claims, such as:

- salary claims that have accrued during the three months before the restructuring or bankruptcy application was submitted to court;
- salary claims that have accrued between the application and the court decision;
- salary claims that have accrued up to one month after the court decision;
- holiday pay claims that have accrued during the current and previous holiday year (that is, 1 April to 31 March if nothing else was agreed between the parties);
- pension claims that have accrued during the previous 12 months; and
- some older claims, because of special rules regarding disputed claims.

The wage guarantee can cover longer time periods if, among other things, the employees are dismissed or if a restructuring is followed by a bankruptcy.

If salaries are covered by the wage guarantee, the state's claim is not prioritised as the employee's claim would have been.

**Pension claims****35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Pension claims against a former employer are prioritised for a period of six months before and six months after the filing for bankruptcy or reorganisation.

Payments into pension plans carried out during the employment are considered as ordinary salary claims in insolvency proceedings and are prioritised, and covered by the wage guarantee as described in question 34.

**Environmental problems and liabilities****36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

The company conducting business on a property bears the primary responsibility for environmental problems. This means that the debtor, and not the bankruptcy estate, is normally responsible.

In some cases the estate may be responsible for environmental costs, for example, for waste stored on a property and for filing reports to the authorities. There is a particular risk of responsibility if the bankruptcy estate continues the business of the debtor.

A claim regarding environmental costs against the debtor is normally treated as any other claim in the bankruptcy, but, as described above, in some cases a claim arises against the bankruptcy estate. In

these cases the environmental costs are preferred claims that are paid before any dividend is distributed to the creditors.

**Liabilities that survive insolvency proceedings****37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

There are no surviving liabilities in a bankruptcy situation with regard to legal entities. The liabilities of a purchaser of the debtor's assets depend on the agreement of the purchaser and estate. If the debtor however is an individual, all liabilities survive.

In a reorganisation, the liabilities will survive unless there has been a voluntary or involuntary composition.

**Distributions****38 How and when are distributions made to creditors in liquidations and reorganisations?**

When the property of the debtor has been converted into money and the creditors are known, the trustee must draw up a dividend proposal. This proposal is announced and gains legal force after three weeks, unless objections to the proposal are made. The district court then confirms the dividend payable and payment can be made.

If a public composition has been declared the court may, upon the request of a creditor, appoint a suitable person (usually the administrator) to ensure that the debtor fulfils his or her undertakings pursuant to the composition by seeing, for example, that it pays claims in accordance with the composition. The time when payments should be made is not regulated in the Reorganisation of Business Act, but will be specified in the composition itself.

**Transactions that may be annulled****39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Recovery in a bankruptcy is principally possible in respect of:

- transactions by virtue of which a creditor has been improperly favoured or the debtor's property has been put out of the reach of the creditors, or his or her debts have been increased;
- gifts;
- unreasonably high salary payments;
- payments of debts in the period beginning three months (two years for affiliated companies) before the day before the petition for bankruptcy was filed (the 'limitation date') and that have been made by non-customary means, prematurely or that are of sums that have caused a substantial deterioration in the financial position of the debtor; and
- conveyance of security less than three months (two years for affiliated companies) before the limitation date, unless such security was necessary at the time the debt arose or has not been conveyed without delay.

Transactions described in the first point above are regarded as null if they took place five years prior to the limitation date and the recipient knew or ought to have known of the debtor's insolvency and the circumstances that made the transaction improper. If the transaction took place more than five years before the limitation date, it will only be regarded as null under the above circumstances if the transaction concerned a person related to or associated with the debtor.

A gift is treated as null if it is made less than six months prior to the limitation date. Gifts made more than six months, but less than a year prior to the limitation date or, if made to a related or associated person, less than three years prior to the limitation date, are treated as null unless it can be shown that the debtor retained property capable of being seized and obviously covering its debts after the gift was made.

Payments of salaries and the like made less than six months before the limitation date and that obviously exceed what was reasonable are treated as null so far as the excess is concerned. Payments made to related or associated persons less than three years prior to the limitation date can be recovered.

Payments of debts made in the time period described above are treated as null unless such payment can be regarded as ordinary in the circumstances of the case at hand. In such a case, a related or

### Update and trends

In accordance with the new scope of the Insolvency Regulation on Insolvency Proceedings (2015/848), that is, to facilitate restructuring of businesses that are considered to have the financial capability to survive and various forms of debt reconstruction procedures for individuals, the *skuldsanering* (debt reconstruction procedure for individuals) under the Debt Reconstruction Act 2006 has been included in the regulation.

Following a debt reconstruction, the debtor is wholly or partially released from the liability of paying the debt covered by the debt restructuring. During the procedure creditors are not allowed to seek payment through enforcement.

Debt reconstruction is decided by the Swedish Enforcement Agency after application from the individual. The prerequisites for

approval are that the individual is domiciled in Sweden, is insolvent and not likely to pay the debt within the foreseeable future and that a granted application is reasonable with regard to the debtor's personal and financial circumstances.

A new regulation regarding debt reconstruction will become effective on 1 November 2016. The new regulation will make it possible for more people to apply for and undergo debt restructuring and will include a certain possibility for business owners.

Furthermore, a bill has recently been presented that is proposed to complement existing laws, in order to comply with the new EU Regulation on Insolvency Proceedings.

associated person may be subject to recovery in respect of transactions occurring within a period commencing two years prior to the limitation date, unless it can be shown that the debtor was not insolvent and did not become insolvent as a consequence of the transaction.

With regard to securities described above, a related or associated person may risk recovery of such security received up to two years prior to the limitation date, unless it can be proved that the debtor was not insolvent and did not become insolvent as a consequence of the conveyance.

The recovery provisions in the Bankruptcy Act regarding fraudulent or preferential transfers also apply when the court has decided that a business reorganisation is to take place and a public composition has been established.

### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The closest thing to 'suspect period' under Swedish law is the rules concerning recovery in the Bankruptcy Act described above. Generally, transactions can only be declared null and void if they have taken place at a time when the debtor is insolvent. There are examples of situations where insolvency is not necessary. Payments of debts, for instance, during the period starting three months (two years for affiliated companies) before the limitation date and that have been made by non-customary means, prematurely or that are of sums that have caused a substantial deterioration in the financial position of the debtor, are recoverable unless such payment can be regarded as ordinary in the circumstances of the case at hand. Another example is gifts (or comparable transactions). A gift can be recovered for quite a long period unless it can be shown that the debtor retained property capable of being seized and obviously covering its debts after the gift was made.

The trustee has the primary right to demand recovery. With the trustee's acceptance, a creditor can challenge a voidable transaction. Assets recovered by the creditor have to be handed over to the bankruptcy estate. Recovery is also possible in formal reorganisations.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Under the Swedish Companies Act, company directors are personally liable for debts arising after a balance sheet for liquidation purposes ought to have been drawn up (when less than half of the company's share capital remains). Personal liability is also possible for debts arising a certain time after the point when the annual report should have been filed with the Swedish Companies Registration Office. Participation in unlawful dividends could also lead to personal liability.

In addition, company directors may be personally liable for unpaid taxes and duties if they have negligently failed to pay them. This probably does not apply if the company has effectively suspended payments before the taxes became due for payment.

Under Swedish law, liability for the debts of affiliated companies will rarely arise, though there have been a number of isolated court cases regarding such liability. It should also be noted that company directors may be subject to penalties and trade prohibition under certain conditions. See also question 13.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Affiliates are generally not responsible for the liabilities of other affiliates unless some sort of guarantee has been issued regarding the particular liability. Piercing the corporate veil has only occurred in very rare cases to date, and appears limited to situations in which there has been a significant lack of financing of the insolvent company, making it solely dependent on the parent company, and the companies have acted improperly in some way.

In Sweden the court is not involved in the distribution of assets. The trustee is responsible for the distribution to creditors, which is conducted in accordance with the rules in the Rights of Priority Act. There are no certain rules regarding group companies, thus each separate enterprise is subject to the relevant insolvency proceeding and claims held by group companies are not treated differently from other claims.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Generally, there are no restrictions, except regarding salary claims, which are not prioritised if they are held by an employee that, alone or together with affiliates, has owned a significant share of the debtor in the six months prior to the filing of bankruptcy or reorganisation, and has had significant influence over the business of the debtor. Since these claims are not prioritised, they are not covered by the wage guarantee.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Enforcement by way of seizure of assets of the debtor, executed by the Enforcement Authority, is possible under Swedish law, but a writ of execution is needed for the creditor. A writ of execution may be obtained through summary proceedings (if not disputed) at the Enforcement Authority or through normal court proceedings.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

As mentioned in question 1, a company may be liquidated according to the rules in the Swedish Companies Act. Such liquidation is conditional on the company being solvent or with consent from the creditors. The meeting of the shareholders then decides whether the company will be liquidated.

In such a liquidation process, a company is dissolved and its assets are converted into cash to the extent necessary, paying off its debts and distributing any surplus to the shareholders. When a company decides to liquidate, its board of directors and managing director represents it until one or more liquidators have been appointed. From then on the liquidator, who replaces the board and managing director, represents the company. The task of the liquidator is to execute the liquidation (wind up the company to the point where it is finally dissolved).

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#### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

A bankruptcy is concluded once the dividend proposal has been declared by court order. With regard to business reorganisations, the court declares it concluded when the purposes of the reorganisation can be regarded as fulfilled. The court can declare the conclusion in the following circumstances:

- if the debtor has failed to appear at the meeting with the creditors;
- in certain circumstances at the debtor's request;
- upon request of the administrator or a creditor, should it not be possible to fulfil the purposes of the reorganisation; or
- should there be any other particular reasons for the business reorganisation to be concluded.

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#### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

There are no statutory provisions regarding recognition of foreign representatives – they are not treated differently from domestic creditors. A foreign bankruptcy estate is, in general, granted legal capacity and party capacity. There is no entitlement to legal aid in such cases. Foreign creditors and foreign claims are recognised in the same way as Swedish creditors and claims. Foreign judgments or orders are only recognised to the extent that statutory provisions so specify.

Normal declaratory judgments in property disputes cannot, in general, be enforced in Sweden without a Swedish writ of execution.

This writ of execution can be obtained based on the European Council Regulations of 22 December 2000 on jurisdiction and the recognition and enforcement of judgments in civil and commercial matters. The Brussels Convention of 27 September 1968 on enforcement and recognition of judgments as well as the Lugano Convention of 16 September 1988 have also been ratified by Sweden.

Adoption of the UNCITRAL Model Law does not appear to be close at hand.

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#### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

In our opinion, the Swedish courts follow the rules of the Insolvency Regulation, along with the decisions of the European Court of Justice.

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#### Cross-border cooperation

#### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

There are no national rules in place in this respect, but the Swedish courts follow the rules of the Insolvency Regulation.

We are not aware of any cases where Swedish courts have refused foreign proceedings or cooperation with foreign courts. This is generally not considered a practical problem in Sweden.

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#### Cross-border insolvency protocols and joint court hearings

#### 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

The Swedish courts have not, to our knowledge, entered into any cross-border insolvency protocols or other arrangements.



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## Legislation

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### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

In Switzerland, the Debt Collection and Bankruptcy Act of 1889 (DCBA) governs the enforcement of pecuniary claims and claims for the furnishing of security against private individuals and legal entities of private law. In 1994, this Act was partly revised and the amendments entered into force on 1 January 1997. A further amendment (which also relates to certain sections of the Code of Obligations and other federal acts) was enacted on 21 June 2013, which came into force on 1 January 2014. The respective amendments are reflected herein. The DCBA is supplemented by other federal statutes, including:

- the Federal Civil Code of 10 December 1907, amended on 25 September 2015;
- the Federal Code of Obligations of 30 March 1911, amended on 20 June 2014;
- the Private International Law Act of 18 December 1987 (PILA), amended on 19 June 2015;
- the Federal Act Regarding Merger, Demerger, Conversion and Transfer of Assets and Liabilities of 3 October 2003 (the Merger Act), amended on 23 December 2011;
- the Swiss Federal Banking Act of 8 November 1934 (SFBA), amended on 19 June 2015, the Ordinance of the Swiss Financial Market Supervisory Authority (FINMA) on the Insolvency of Banks and Securities Dealers of 30 August 2012 (BIO-FINMA), amended on 3 December 2015;
- Swiss Stock Exchange and Securities Trading Acts of 24 March 1995 (SESTA), amended on 19 June 2015, in particular article 36a;
- the Ordinance of FINMA on the Insolvency of Collective Investment Schemes of 6 December 2012;
- the Ordinance of FINMA on the Insolvency of Insurance Companies of 17 October 2012;
- the Collective Investment Schemes Act of 23 June 2006 (CISA), amended on 25 September 2015;
- the Penal Code of 21 December 1937, amended on 20 June 2014, in particular the prescriptions regarding crimes and offences in debt enforcement and bankruptcy, fraudulent bankruptcy and pledge fraud;
- the Federal Insurance Contract Act of 2 April 1908, amended on 19 December 2008;
- the Federal Act on the Mandatory Unemployment Insurance and the Indemnity for Insolvency of 25 June 1982, amended on 20 June 2014;
- historic bankruptcy treaties of the 19th century, such as the Bankruptcy Treaty of 1825/1826 between all Swiss cantons (except Schwyz and Neuenburg) and the (former) kingdom of Württemberg (currently valid for the district of the Oberlandesgericht Stuttgart) or the Bankruptcy Treaty of 1834 between most of the Swiss cantons and the (former) kingdom of Bavaria on consistent handling of mutual citizens;
- specific rules regarding the foreclosure of aircraft or vessels, which to a large extent follow the provisions of the Ordinance

on Foreclosure of Real Properties of 23 April 1920, amended on 23 September 2011;

- the Lugano Convention on the Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters 1988 (the Lugano Convention) as revised 30 October 2007, effective as of 1 January 2011, which is not per se bankruptcy-related but has a substantial impact when it comes to the enforcement of judgments;
- the Swiss Code of Civil Procedure (CPC), which replaced the former 26 cantonal procedure codes, of 19 December 2008, amended on 19 June 2016; and
- the Federal Act on Data Protection of 19 June 1992, amended on 1 January 2014.

In the case of a corporate debtor (corporations, corporations with unlimited partners, limited liability companies and cooperatives), over-indebtedness is the most frequent criterion for the beginning of insolvency. Over-indebtedness means the liabilities of the company are not covered whether the assets are appraised at ongoing business value or at liquidation value. Also, a declaration of illiquidity in the sense of article 191 of the DCBA by a debtor (whether corporate or individual) initiates insolvency proceeding.

Notably, insolvencies of banks, securities dealers, mortgage bond clearing houses, insurance companies, collective investment scheme companies (SICAFs and SICAVs, and limited partnerships for collective investments) and fund managers will be dealt with by the Swiss Financial Market Supervisory Authority (FINMA) according to the special insolvency rules, as applicable. The respective rules are not discussed further herein.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Debt enforcement against legal entities takes place at their registered seat as reflected in the commercial register. The bankruptcy court in the district where the enforcement proceeding was begun is competent to adjudicate the opening of the bankruptcy in a summary proceeding. Bankruptcy proceedings in Switzerland can be carried out at one place only. Following the principle of 'unity of bankruptcy proceedings' they are deemed opened at the place where the debtor was first declared bankrupt. A change of domicile of a debtor has no effect on the venue once the bankruptcy warning has been served.

As the case is automatically transferred to the bankruptcy office after the declaration of bankruptcy by the court, the involvement of the bankruptcy court is limited. The bankruptcy court may ex officio transfer a case to the composition judge for examination of a possible composition agreement and will stay in charge if a corporate moratorium proceeding pursuant to article 725a of the Code of Obligations is applied for.

FINMA has judicial authority for institutions qualified under the SFBA and BIO-FINMA.

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**Excluded entities and excluded assets**


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**3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?**

A debtor in bankruptcy may be any person or entity registered in the commercial register with one of the following capacities:

- an individual owning a business;
- a member of a partnership;
- a member with unlimited liability of a limited partnership;
- a member of the board of a partnership limited by shares;
- a partnership;
- a limited partnership;
- a company or partnership limited by shares;
- a partnership with limited liability;
- a cooperative;
- an association;
- a foundation;
- a trust;
- an investment company with variable or fixed capital (SICAV or SICAF); or
- a limited partnership for collective investments.

A debtor who is not registered in the commercial register is subject to individual debt collection, but will also be adjudicated bankrupt if articles 190 to 194 of the DCBA apply.

Debt collection by means of bankruptcy proceeding is in all events excluded for taxes, duties, contributions, emoluments, fines and other obligations based on public law and owed to public treasuries or officials.

In general, all assets belonging to the debtor that have a monetary value form part of the insolvent estate. Assets that qualify as purely personal assets and that do not qualify for seizure are exempt. In the case of an individual debtor this also applies to benefits under a pension plan which are not yet due. Third-party assets in possession of the debtor may be segregated for the benefit of such third party. Under the SFBA and BIO-FINMA specific rules apply to protect bank customer deposits and claims.

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**Public enterprises**


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**4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?**

In principle, the insolvency proceedings of fully or partially government-owned enterprises are also governed by the procedure stated by the DCBA (ie, irrespective of whether an enterprise is owned by the government or not the same rules apply. The insolvency of government-owned banks (eg, the government-owned cantonal banks and PostFinance) is – like other banks and securities dealers – additionally governed by the restructuring and bankruptcy procedure of BIO-FINMA. For shipping and railway companies – whether governed-owned or not – the Pledge and Compulsory Liquidation of Railway and Shipping Companies Act of 1917 applies.

Federal and cantonal laws can, however, stipulate exceptions for specific types of government-owned enterprises. One such exception are entities established under public cantonal law whose insolvency is primarily governed by the Debt Collection Against Communities and Other Entities of Public Cantonal Law Act of 1947. The rules of the DCBA may only be applied subsidiarily. Such entities are in particular not subject to the bankruptcy proceeding under the DCBA. Only debt collection by realising pledged property or seizure of assets is possible. However, assets needed for fulfilling public tasks (administrative assets) including tax assets may not be seized. Seizable are therefore only the financial assets of the public entity. The Swiss Confederation and its public institutions are subject to debt collection under the DCBA but seizure is also limited to financial assets.

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**Protection for large financial institutions**


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**5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered ‘too big to fail’?**

Following the rescue of UBS in 2008, different legislative projects were started in order to avoid further public bailouts of banks. In the

meantime, Switzerland has enacted comprehensive legislation. In April 2010, the two major Swiss banks (UBS and Credit Suisse) were identified by a commission of experts as companies ‘too big to fail’ in Switzerland. In 2013 and 2014, two other Swiss banks, the Zürcher Kantonalbank (November 2013) and Raiffeisen (June 2014), were declared systemically important by the Swiss National Bank. In September 2015, PostFinance, a wholly owned subsidiary of the government-owned Swiss Post, was added as number five to the list of systemically important banks.

During the same period, the Swiss banking law was partially revised. Systemically important banks are obliged to increase their equity by 2018 and to ensure essential political economic functions if they go bankrupt. The new banking law provides for contingent convertible bonds (Coco-Bonds). More stringent requirements on capital, liquidity and risk have been imposed to limit the risks of systemically important banks. The respective provisions entered into force on 1 March 2012. Pursuant to the Liquidity Ordinance (LiqO), effective since 2012, banks are obliged to manage and monitor liquidity risks appropriately. On 25 June 2014, the LiqO was revised and supplemented by quantitative liquidity requirements in accordance with the international liquidity standards. The amendments came into force on 1 January 2015.

On 1 November 2012, FINMA replaced the former Bank Bankruptcy Ordinance with the Banking Insolvency Ordinance (BIO-FINMA). BIO-FINMA consolidates the implementing provisions governing the restructuring and bankruptcy procedure for banks and securities dealers into a single decree. It completes Swiss legislation on insolvency and crisis prevention and meets international requirements. BIO-FINMA contains detailed regulations on the restructuring process, while the bankruptcy provisions were adopted practically unchanged from the former Bank Bankruptcy Ordinance. The expectation is that BIO-FINMA will make the restructuring and bankruptcy process both rapid and effective, taking proper account of individual cases, and preserving legal certainty. BIO-FINMA contains detailed regulations on the restructuring powers available to FINMA. In particular, instead of restructuring an entire bank, FINMA has the option, to ensure the continuation of individual core banking services, to convert debt capital into equity capital and to prescribe other corporate actions.

On 1 January 2013, the revised Banking Ordinance and the Capital Adequacy Ordinance entered into force. As a result, banks must comply with the new rules of the Basel Committee on Banking Supervision (Basel III). Moreover, big banks whose failure would considerably harm the Swiss economy must comply with supplementary capital and risk diversification requirements, as well as presenting an effective emergency plan to the supervisory authority. On 30 April 2014, the Banking Ordinance was totally revised. This revision, together with a partial revision of the Banking Act (SFBA) and the revised provisions of the Capital Adequacy Ordinance, came into force on 1 January 2015. With the revision of the Banking Ordinance, the new accounting legislation (accounting standards) and the regulations regarding unclaimed assets were implemented.

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**Secured lending and credit (immovables)**


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**6 What principal types of security are taken on immovable (real) property?**

A debtor may provide its creditors with a variety of forms of security and quasi-security interests. With regard to charges on immovable property, the subject matter of the security is real estate within the meaning of article 655(2) of the Civil Code. A real estate security interest can be established in only two ways: as a mortgage or real estate bond. Detailed provisions regulate these different types of security interests. Such ‘real estate security interest’ has to be recorded in the land register.

Real estate interest may only be established for a specified amount of the claim denominated in Swiss currency. If the amount of the claim is not or cannot yet be determined, the parties can fix a maximum amount. Likewise, interest charges need to be fixed by the parties and are subject to the permissible maximum interest rate fixed by cantonal legislation.

Pursuant to a partial revision of the Federal Civil Code, which became effective on 1 January 2012 as an alternative to the present real estate bond, a paperless register bond has been established. The paperless register bond comes into existence with an entry in the land register.

## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

As regards moveable property, various means are on hand to secure a claim:

- right of retention (security interest) – a right to satisfy a claim by enabling a creditor (with the consent of the debtor) to retain and sell moveable property or securities that are in his or her possession, and that the creditor would otherwise be obliged to surrender. The creation and continuation of the right of retention is dependent upon possession of the moveables. If the debtor fails to fulfil his or her obligation, the creditor may, if he or she is not sufficiently secured, realise the retained asset, following prior notification of the debtor, in the same manner as a pledge; and
- pledges – to secure a present or future claim, moveable goods can also be pledged. Delivery of possession of the specific moveables to the creditor or to a third person holding the pledge for the creditor is a prerequisite.

The two security rights differ primarily in that the right of pledge is usually based on a contract, whereas the right of retention is also of statutory nature and can therefore be applied without a specific contract:

- retention of title – frequently, general business terms and conditions will provide for a retention of title by the seller of goods until the purchase price is fully paid. It is necessary for the parties to explicitly agree upon such a retention of title and the goods concerned have to be registered item by item in the Public Retention Title Register (Civil Code, article 715). Swiss law presumes that the possessor of goods is the legal owner. The registration does not prevent a transfer of the property title to a third party that acts in good faith. The entitled creditor is, however, protected in the case of seizure of the goods or bankruptcy of the debtor; the monitoring of the register of title retention is cumbersome, with the consequence that this security instrument is not widely used. If moveable property arrives in Switzerland and is subject to a reservation of title validly established abroad but for which the requirements of Swiss law are not yet satisfied, the retention of title will remain effective in Switzerland for a period of three months (PILA, article 102(2));
- fiduciary transfer of property title – in practice, full property title of an asset is often vested in the creditor (or a third party) with the understanding that the asset serves as security only. A fiduciary relationship is thereby created, by which the holder of the property enjoys the legal position of a proprietor but the transfer is connected with the (implied or explicit) contractual obligation to act in the best interest of the principal and to return the property once the contractual obligations are met; and
- person-related securities – the creditor may seek an undertaking from a third party to pay the debt (or secure the specific performance) of the primary debtor. Types of such undertakings are:
  - undertaking of a guarantee (Code of Obligations, article 111); and
  - undertaking as a suretyship (Code of Obligations, articles 492 et seq). Because of the strict formalities to be observed in the case of a suretyship and its similarity to a guarantee, the parties have to be attentive when employing these security instruments. The suretyship must in all cases specify the maximum amount of liability and must be recorded in a notarised deed if issued by a natural person.

## Unsecured credit

### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

A simple statement of the creditor to the debt collection office at the debtor's domicile or at the debtor's registered office is sufficient to commence the enforcement proceedings of a money claim. Upon receipt of the enforcement request, the enforcement office issues the summons to pay. The debtor can file an objection within 10 days of notification without giving reasons. This forces the creditor to set aside the objection and, depending on the evidence at hand on the claim, to:

- institute an ordinary legal action (in the event of liquid cases in a summary proceeding) to prove the claim;
- request, in a summary proceeding;
- the enforcement of an enforceable judgment rendered by a Swiss court, or an equivalent order of a recognised foreign court, in which case the court will definitively set aside the objection; or
- reach a provisional setting aside of the objection if the claim is evidenced by a written debt acknowledgement duly signed by the debtor.

Considerable case law has been developed to establish what qualifies as such debt acknowledgement. In this instance, the debtor can resort to ordinary legal action to quash the summary decision. Pursuant to the Swiss Civil Procedure Code (CPC), the setting aside of the objection can become definitive, as in the case of an enforceable decision, provided the debt acknowledgment is established by way of a notarial deed.

A fast-track proceeding is available to creditors who hold on to a bill of exchange or a cheque.

If the debtor neither pays nor objects in a timely manner, or if the creditor has successfully set aside the objection raised by the debtor, the creditor is entitled to apply for the continuation of the enforcement proceeding after 20 days, at the earliest, since the summons to pay has been served. If successful, the creditor may then continue the debt collection proceeding by filing a bankruptcy petition, or, if the debtor is not subject to bankruptcy proceedings, to have the debt collection office seize enough of its assets to cover the claim (other creditors who file their own request of continuation within 30 days of a seizure will participate in the proceeds realised from the seized assets). A new debt collection proceeding must be started if the proceeding is not continued within one year from service of the payment order, not counting the period used for the setting aside of the objection.

Whereas the purpose of the bankruptcy proceedings is to realise all of the assets of the debtor to satisfy out of the proceeds the claims of all of the creditors in accordance with their secured rights and priorities, the seizure procedure is for individual creditors and aims at realising only certain assets of the debtor.

### Pre-judgment attachment proceeding

A special asset freeze proceeding is provided for under articles 271 et seq of the DCBA. In connection with the revised Lugano Convention, effective as of 1 January 2011, the regime for freezing orders has been modified and its scope has been extended. Freezing orders are available for both local as well as foreign creditors; they are subject to specific prerequisites. Such a freezing order has to be applied for by the court of the place where a debt collection against a debtor can be initiated or at the place the asset is located. It will be granted upon demonstrating prima facie evidence of a liquid and due but unsecured money claim. The creditor has to plausibly demonstrate to the court in a summary ex parte proceeding where the assets to be attached are located; 'fishing expeditions' are unlikely to be heard. However, pursuant to the revised law, the court can now issue freezing orders for the entire territory of Switzerland. This is a substantial improvement as before several orders needed to be obtained if the assets were kept in different local districts.

Freezing orders can be applied against assets located in Switzerland belonging to debtors resident abroad. Unless other grounds of attachments apply, respective claims must be based on an enforceable court decision or arbitral award or a debt acknowledgment or must at least be sufficiently connected with Switzerland. This sufficient connection test was introduced by the more recent partial revision of the DCBA and is subject to qualification by case law. With the revised Lugano Convention and related revision of the DCBA, any creditor holding an enforceable judgment, be it from a Swiss court or from a court of a member state of the European Union (or of the Lugano Convention, such as Norway or Iceland), or having a notarised debt acknowledgment at hand, will have the right to request a freezing order against a Swiss debtor. The freezing order is now recognised as the protection measure to be provided for under article 47 paragraph 2 Lugano Convention. The revised law also has introduced the possibility for the debtor to file a pre-petition protection letter to challenge an application for a freezing order.

The effects of a freezing order are to provisionally secure assets for the specific creditor. The freezing order is subject to challenge by the debtor. The creditor is liable for damages resulting from an unjustified attachment and must, to maintain the attachment, pursue a validation

proceeding in a timely manner. During a legally determined period, creditors who likewise qualify may join in the proceeding and, thus, frustrate the result of the first attachment.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Corporate law provides for the dissolution procedures for legal entities leading to a voluntary liquidation of the business with full protection of the creditors' claims.

Upon their own motion, bankruptcy proceedings may be opened against companies limited by shares, partnerships limited by shares, partnerships with limited liability and cooperatives without prior enforcement proceedings in the instances provided for by the Code of Obligations (articles 725a, 764(2), 817 and 903). The application is based on a demonstration of manifest (ie, not just temporary) insolvency and is to be supported by a shareholders' resolution and a recently established balance sheet.

As the voluntary liquidation leads to a bankruptcy proceeding, its effects do not differ from those in an involuntary liquidation as described below. Debtors that are not otherwise subject to bankruptcy proceedings may request its application upon declaration of insolvency.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

To place a debtor in an involuntary proceeding, the creditor must have complied with the preliminary debt collection procedure that involves the issuing and notification of a payment order by the debt collection and bankruptcy office at the request of the creditor, a successful setting aside of a possible objection raised by the debtor in a summary procedure and the petition to continue the execution. If the creditor has complied with the above, a bankruptcy warning is issued by the debt collection and bankruptcy office.

At this point in time, the bankruptcy court, at the creditor's request, may order as a protective device the drawing up of an inventory of all the debtor's assets. If the claim is not satisfied 20 days after the service of the bankruptcy warning, the creditor can apply to the bankruptcy court to declare the opening of the bankruptcy. The bankruptcy order marks the start of the bankruptcy proceeding to be conducted by the bankruptcy office and results in a general execution with all its civil and procedural legal effects.

A creditor may request the court to declare a debtor bankrupt without prior enforcement proceedings if the whereabouts of the debtor are unknown, or if the debtor evades its liabilities, engages in fraudulent conduct, has concealed assets in a preceding debt collection, or has ceased to make payments.

The declaration of bankruptcy can be suspended by the court if a petition for a debt moratorium, emergency moratorium or, alternatively (but only for stock corporations, limited liability companies and cooperatives), for a corporate moratorium pursuant to article 725a of the Code of Obligations is submitted.

The start of a bankruptcy liquidation has the following effects:

- one single bankrupt estate is formed consisting of all assets to which the debtor is entitled (irrespective of where they are located or whether they serve as security). The right to dispose of the assets is automatically transferred to the bankruptcy administration. The administration office establishes an inventory of all assets and takes protective measures;
- other enforcement proceedings directed against the debtor are automatically suspended and, in general, pending litigations will be suspended as well;
- all obligations of the debtor become due against the bankrupt estate with the exception of those secured by mortgages on real estate;
- except for claims secured by pledge, interest ceases to accrue against the debtor;
- claims subject to a suspensive condition are admitted in their full amount in the bankruptcy;
- claims that are not for a sum of money have to be converted into a monetary claim of corresponding value;

- a creditor may set off its claim against a claim that the debtor has against him or her, provided that obligation was contracted bona fide prior to the opening of the bankruptcy; and
- the creditors' claims are ascertained and listed in the schedule of claims by order of ranking and secured rights.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

A composition proceeding is a measure to protect the debtor from the consequences of bankruptcy. It allows the debtor to postpone payment of the debts or to satisfy them in total or in part, according to a specific plan. The proposed composition agreement must be ratified by the creditors. According to the newly amended DCBA, the Swiss composition procedure is now designed to rehabilitate the company under the auspices of the court or to reorganise unsecured and unprivileged claims.

Any debtor, whether subject to a bankruptcy proceeding or not, seeking to reach an agreement with its creditors, may initiate a debt moratorium proceeding by submitting to the court a reasoned application enclosing recent financial statements and a liquidity plan together with relevant documentation demonstrating the current and future financial status of the debtor as well as a provisional rehabilitation plan. Usually, the composition court will request additional documentation.

A temporary debt moratorium not exceeding four months may be granted by the court. To protect the debtor's assets, the court will implement the necessary conservatory measures. Should the court conclude that is unlikely that rehabilitation or the conclusion of a composition agreement with creditors will be successful, the court will open bankruptcy proceedings. At the discretion of the court, one or several provisional commissioners for the temporary debt moratorium may be appointed for the purpose of assessing the viability of the debtor's proposal. Provided all third-party interests remain protected, the court may abstain from making a public notice of the temporary debt moratorium (in which case the appointment of a commissioner is mandatory). In essence, the effects of the temporary debt moratorium are the same as for the definitive debt moratorium. If the temporary debt moratorium shows that a rehabilitation of the debtor or conclusion of a composition agreement with its creditors can be expected, the court, acting *ex officio*, may grant a definitive debt moratorium for an additional four to six months and will appoint one or more commissioners. The commissioner's primary duties are to supervise the debtor's activities and to perform the tasks set out in articles 298 to 302 and 304 of the DCBA. The actual powers of the commissioner will be determined case by case and can involve actual managerial powers. The commissioner has to present interim reports at the request of the composition court and has to inform the creditor of the progress of the moratorium. The definitive moratorium may be extended from the usual period (four to six months) to 12 months and, in complex cases, 24 months. Depending on the circumstances, the court can establish a creditors' committee, which will act as a supervisory body for the commissioners. The creditors' committee should be composed of representatives of the various classes of creditor. Once established, the creditors' committee will decide on the sale or charges of assets.

The effects of a provisional and temporary debt moratorium are the suspension of all pending execution proceedings including bankruptcy and asset-freezing orders (but the prosecution of claims secured by a mortgage remains possible without the realisation of the asset). Emergency provisions, and civil and administrative litigations will be suspended. As one of the centrepieces of the amended DCBA, subject to the express consent of the commissioners and provided the rehabilitation would otherwise be jeopardised, the debtor is entitled to terminate long-term contracts. Resulting (damage) claims will become subject to the composition agreement.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

The possibility for creditors to commence involuntary reorganisation in Switzerland was only introduced by the DCBA revision in 1994. In practice, the demand for reorganisation by creditors is not very frequent. The main prerequisite for creditors to commence an involuntary

reorganisation is the creditor's right to request the opening of bankruptcy proceedings according to article 166 or 190 of the DCBA. In addition, the court may also stay judgment on the opening of bankruptcy proceedings of its own motion if it appears that an agreement will be reached with the creditor. In this case, the file will be transferred to the composition court.

Apart from that, the effects of involuntary reorganisations do not differ from those for voluntary reorganisation.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

Over-indebtedness forms a special cause of bankruptcy for corporations, corporations with unlimited partners, limited liability companies and cooperatives.

Over-indebtedness means the liabilities of the company are not covered whether the assets are appraised at ongoing business values or at liquidation values. To maintain going concern value a sound cash-flow plan securing the operation for a reasonable period will be requested.

As long as at least half of the equity capital still exists, an adverse balance sheet remains unremarkable. But if the previous annual balance sheet shows that half of the share capital and the legal reserves are no longer covered, the board of directors must without delay call a general meeting of shareholders and propose a financial reorganisation.

If there is substantiated concern of over-indebtedness, an interim balance sheet must be prepared and submitted to the auditors for examination. If the concern is approved, the company bodies (board of directors, liquidators, auditors) are obliged, in the interest of the creditors, to notify the judge (Code of Obligations, article 725(2)). This notification of over-indebtedness is generally referred to as 'dumping of the balance sheet'. The timeline of the filing is decided on a case-by-case basis; in light of recent court cases the breathing period tends to be restricted to a couple of weeks.

Notification of over-indebtedness may only be avoided if the balance sheet can be reorganised within a short time, in particular because creditors of the company subordinate their claims to those of all other company creditors to the extent of such insufficient coverage.

After a summary examination of over-indebtedness, the judge adjudicates the bankruptcy *ex officio*. Despite over-indebtedness, the judge may refrain from or postpone adjudicating the bankruptcy in two cases:

- if there is a possibility of a financial reorganisation, in which case he will take appropriate measures to preserve the value of the assets; or
- if there are indications of accomplishing a composition with creditors.

A bank that no longer fulfils the licensing requirements or violates its legal obligations risks the withdrawal of its banking licence, which inevitably results in the liquidation of the bank. In these situations, or if the bank is threatened by insolvency, FINMA has authority under the SFBA, which was revised in several steps most recently on 22 March 2013 to order far-reaching protective measures or the restructuring of the bank. The appointment of an independent expert investigator by FINMA so as to examine certain matters within the bank or to monitor the implementation of measures imposed by FINMA are among those protective measures. Also, a restructuring administrator can be appointed by FINMA to establish a restructuring plan. In the case of liquidation, FINMA appoints a liquidator.

The members of the board of directors and all persons engaged in the management or liquidation of the company, as well as all persons engaged in the audit of the annual account, are liable not only to the company, but also to the shareholders and to the company's creditors for the damage caused by an intentional or negligent violation of their duties, for which a disregard of the prescriptions set out in article 725 of the Code of Obligations is being considered. The prescriptions regarding liability (Code of Obligations, articles 752 to 760) also apply to the founders, organs or supervisors of banks.

As a further consequence, certain transactions carried out by the company while insolvent may be subject of avoidance actions (DCBA,

article 287) in order to refer the assets in question to the estate (see question 39).

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

Under the supervision of the commissioner and at the direction of the composition court, the debtor may continue its business operations. However, certain transactions will require approval from the court or the creditors' committee, if appointed. The debtor is prohibited to divest, encumber or pledge fixed assets, to give guarantees or to donate assets without the authorisation of the composition court or the creditors' committee, respectively. Moreover, if the debtor contravenes the commissioner's instructions, the court can revoke the debtor's capacity to dispose of its assets or itself declare bankrupt. At the discretion of the court, the authority to operate the business can exclusively be given to the commissioner. The court may deprive management of its power of disposal or make its resolutions conditional on the consent of the commissioner. Contracts entered into during the moratorium with the approval of the commissioner enjoy priority over pre-petition rights. Unless a creditors' committee is appointed, which is one of the new features of the revised DCBA, the role of the creditors during the entire proceeding is fairly passive. They have to file their claims, can attend the creditors' meeting, can approve or reject the proposed composition agreement and have the right to be heard in court.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

##### Liquidation

Regarding liquidation, there are two effects of the adjudication of bankruptcy with respect to enforcement and legal proceedings. As long as enforcement proceedings against the debtor are affected, all those proceedings cease and new enforcement proceedings relating to claims that arose before the opening of bankruptcy proceedings are not possible (except the enforcement of pledges given by third parties). Those enforcement proceedings for claims that arose after the declaration of bankruptcy can be continued during the bankruptcy proceedings by seizure or by realisation of pledges.

Civil court actions to which the debtor is a party and that affect the composition of the bankrupt estate are stayed, with the exception of urgent matters. In ordinary bankruptcy proceedings they can be resumed, at the earliest, 10 days after the second creditors' meeting. In summary bankruptcy proceedings, they can be resumed, at the earliest, 20 days after the schedule of claims is made available for inspection. Under the same conditions, administrative proceedings are stayed.

##### Reorganisation

As a general effect of composition, all pending execution proceedings, including petitions for bankruptcy and asset freezing, are stayed. Secured creditors may, regarding charges on immovable property, initiate the procedure for the realisation of security, but the charge will not actually be realised. Except for urgent cases, pending civil and administrative proceedings are stayed.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

In accordance with article 204 of the DCBA, one of the main effects of bankruptcy is that the debtor is deprived of all rights of disposal over its assets. The administrator, however, is able to contract new obligations,

such as a loan or a credit, which may touch the free assets of the bankrupt estate.

#### Post-filing credit in reorganisation

Any debt contracted during the debt moratorium with the approval of the commissioner constitutes a debt against the assets in a composition with assignment of assets or in a subsequent bankruptcy proceeding and is, therefore, privileged.

#### Set-off and netting

##### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

With respect to any claim a bankrupt debtor has against a creditor, the latter can exercise a right of set-off. The right of set-off is, however, excluded in the following situations:

- if a debtor of the bankrupt became a creditor only after the opening of the bankruptcy proceeding (except if such a debtor only fulfils an obligation which was pre-existing at the time of the opening of the bankruptcy or if debts of the bankrupt are satisfied by using collateral made available by such a third-party debtor);
- if a creditor of the bankrupt became a debtor of the bankrupt debtor or the bankrupt estate only after the declaration of bankruptcy;
- if the claim to be set off results from unpaid capital contributions.

Set-off against claims generally arises where the creditor establishes that the rights were acquired bona fide prior to the adjudication of bankruptcy. The set-off is voidable where the debtor of a bankrupt debtor has acquired, prior to the opening of bankruptcy but knowing its creditor is insolvent, a claim against him or her, with a view to procure for itself or a third person, by way of set-off, an advantage to the prejudice of the assets in bankruptcy (DCBA, article 214). Regarding composition, the same provisions apply.

While there is some room for cherry-picking by the administration regarding the performance of unfulfilled contracts in general concerning netting, the administrator's right to decide whether to perform contracts concluded by the bankrupt party is excluded under Swiss law (DCBA, article 211) in respect of contracts to be performed at a fixed date as well as in respect of forward, swap and option contracts, provided the value of the obligations yet to be performed can be determined on the basis of a market or stock exchange price. Swiss law further provides that both the administration and the solvent counterparty have the right to claim the difference between the agreed value of the contractual obligations and their market or stock exchange value on the date of the opening of bankruptcy proceedings, which will enable the set-off of the claim arising from such a liquidation procedure against any debt of the other party (as Swiss law allows the set-off of claims that came into existence prior to the bankruptcy judgment).

#### Sale of assets

##### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

#### Sale of assets in a reorganisation

The right of the debtor to dispose of its assets is generally preserved but restricted by the way in which the business activities are supervised by a commissioner. The debtor is prohibited to divest, encumber or pledge fixed assets, to give guarantees or to donate assets without the authorisation of the composition court or the creditors' committee, respectively. Any such transactions if entered into are null and void against creditors. In some cases the judge may authorise the commissioner to pursue business instead of the debtor, which effectively puts the debtor under guardianship. These statutory restrictions will not affect the validity of transactions concluded with bona fide third parties. If the debtor refuses to follow the commissioner's instructions, the court can revoke the debtor's capacity to dispose of its assets or

declare bankruptcy. The amended DCBA now refers to the possibility of establishing a rescue company the shares of which can be used, with approval of the court, to satisfy the creditors.

#### Sale of assets in a liquidation

In liquidation, the debtor loses its right of disposal over its assets as soon as the judge opens bankruptcy proceedings. Although the debtor remains the legal owner of its assets, the right of disposal is transferred to the administration for purposes of their liquidation. As soon as the bankruptcy judgment is published, any unilateral or bilateral transactions concerning assets belonging to the bankrupt estate entered into by the debtor, and not the estate, are void as against its creditors. However, the payment of a promissory note to a bona fide creditor will not be regarded as void, as well as the sale or encumbrance of real estate when the restriction on the debtor's right of disposal is not yet registered in the Land Register.

#### Liabilities

In an acquisition of immovable property, the charges and liabilities registered for that property will generally pass on to the acquirer. To ascertain such charges, a special procedure will be conducted. The acquirer will also inherit existing environmental liabilities subject to possibility of recourse against the former owner. Moveables, instead, will be transferred free and clear of claims. The amended DCBA makes clear that a transfer of a business or part thereof in the course of a debt moratorium, a bankruptcy or a composition agreement with assignment of assets will not automatically result in an assumption of the employees' related liability by the acquirer, but rather such liabilities will be assumed only upon explicit consent by the acquirer.

#### Stalking horse procedure

Swiss bankruptcy law does not provide for a specific stalking horse procedure and the concept does not appear to have been tested in court. In a bankruptcy or insolvency liquidation, the assets are sold by public auction or free sale, as the liquidator may determine. Generally, in the case of real property and other substantial assets, the creditors will be granted a right to participate in the sale process and to make higher bids. While the liquidator has substantial discretion in organising a free sale process, the procedure should be fair in terms of time, should grant equal treatment and should disclose specific conditions of the interim sale agreement.

#### Credit bidding in sales

The sale of assets under any enforcement procedure of the DCBA requires cash payment by the bidder and the sale proceeds will be allocated to the creditors in line with their rankings. Exceptionally, money claims may be transferred at par value to a creditor in satisfaction of the equivalent amount. The courts have also accepted a set-off in specific circumstances for secured claims but only when it was obvious and uncontested that the sales proceeds would have to be handed out to the acquiring creditor. To the extent a transaction is governed by Swiss law, there is no difference whether the original secured creditor or an assignee of the original creditor request a set-off. Private sales, which are typically stipulated in security contracts and which may also provide for a right of the creditor to step in as acquirer, are not enforceable in bankruptcy situations.

#### Intellectual property assets in insolvencies

##### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

Bankruptcy does not result per se in a termination of ongoing agreements, and respective claims that are incurred up to the date of first ordinary termination of the expiration of the contract term can be submitted, whereby benefits accruing to the creditor must be accounted for. The bankruptcy administrator is entitled to step into a contract that is not or only partly fulfilled. So, if considered beneficial for the estate, the bankruptcy administrator will elect a continued performance of

the licence agreement, which will result in a privileged treatment of the accepted claims. If the administrator opts not to step in, the contract party can request appropriate security for the continued performance, and if not provided, terminate the agreement.

It is controversial how the monetary and the non-monetary claims resulting from the licence agreement (which will have to be converted into monetary claims) will actually be treated in the proceeding. It is generally (but not universally) accepted that article 211(2) of the DCBA is a procedural rule only so that contractual clauses addressing termination should be overriding. Such clauses, however, will be tested against avoidance rules. Under the amended DCBA – during the debt moratorium – the debtor is entitled to terminate long-term contracts with the consent of the commissioner if the continuation of the contractual relationship would impede the rehabilitation of the debtor. Compensation for such early termination must be granted but the respective damages claim will be treated as an ordinary creditor's claim.

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### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The sale of personal information or customer data collected by an insolvent company in the course of an insolvency proceeding is not restricted by Swiss insolvency provisions but has to be in compliance with the general rules of the Swiss Federal Act on Data Protection (the DPA). The DPA allows, under certain conditions, the sale of personal information or customer data to a third party.

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### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

The debtor is now allowed to cancel onerous long-term contracts, if their continuation would frustrate the intended rehabilitation. Such early termination requires the consent of the commissioner. Compensation for early termination may be granted but respective claims will be treated as ordinary creditor claim. The special provisions for employment contracts remain reserved. Otherwise, contracts entered into by the debtor prior to the commencement of the respective proceeding remain in force. By operation of law some specific contracts such as a mandate will terminate with the bankruptcy or involuntary liquidation.

While pecuniary claims become due, obligations that are not of pecuniary nature will be translated into a pecuniary claim. Special rules apply for 'synallagmatic contracts' (meaning contracts that involve contractual performances by both parties) that had not or only partially been fulfilled at the time of the opening of the insolvency proceeding. Pursuant to article 211 of the DCBA, the administrator in a bankruptcy can decide whether he or she (in lieu of the debtor who has lost its rights to dispose over assets and contractual rights) wants to fulfil such a contract. The law does not set forth within what time such decision should be made. As consequence, this discretion to 'cherry pick' can create legal uncertainty for the involved party. Contractual clauses to avoid the uncertainty may be considered. As a matter of law such discretion is not warranted in cases of contracts that need to be performed at a specific date as well as for financial future, swap and option transactions if the value of the contractual performance can be determined by a market price. If the administrator chooses to continue with the contract, the adversary party may request security for its performance, and decline the performance if no sufficient security is provided.

Claims resulting from contracts or breach of contracts, respectively, that are fulfilled with the approval of the administrator enjoy privileged treatment. In contrast to that, claims resulting from contracts that were entered into or fulfilled without the approval of the administrator are treated as ordinary creditor claims.

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### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Given the extensive international exposure of the Swiss economy, arbitration issues often arise in collective enforcement proceedings with a Swiss context. The availability of and the limitations to arbitration in connection with insolvency proceedings are subject of continued legal discussion. The admissibility of arbitration is largely dependent on the nature of the specific dispute and on whether the bankruptcy trustee or receiver is bound by a given pre-existing arbitration clause. Whereas for Swiss international arbitration (where the seat of the arbitration is in Switzerland but at least one party is domiciled abroad) a matter is arbitrable if the dispute involves 'an economic interest' (PILA, article 177(1)), in Swiss domestic arbitration the test is whether the parties are free to dispose of the rights of the dispute (CPC, article 354). In the first case, the concept is of a liberal nature but is restricted by public policy, while in cases of domestic arbitration the limitations are posed by the mandatory rules of collective enforcement. Despite the liberal concept of arbitrability in Swiss international and domestic arbitration law, certain types of insolvency proceedings cannot be argued before an arbitral tribunal. This especially relates to the actions which exclusively aim at enforcing debts, such as the creditor's application to the court to (definitively or provisionally) set aside the debtor's objection in summary proceedings (DCBA, articles 80 to 84). Since an arbitration process can only replace the ordinary judicial proceedings, but not (administrative) enforcement proceedings, in relation to the DCBA only actions of substantive nature (such as the action for contested claims in composition proceedings pursuant to article 315 of the DCBA) and, according to the dominant Swiss doctrine, actions with a reflexive effect on substantive law (such as clawback claims pursuant to the articles 285 to 292 of the DCBA), respectively, are considered as arbitrable.

In practice, the possibility to arbitrate is often decided by the circumstances whether the trustee or receiver in a bankruptcy takes the role of a defendant or rather acts as plaintiff. It is still questioned whether parties may validly agree to resolve a dispute regarding a voidance action by arbitration.

Although still a matter of debate, it seems widely established meanwhile that an arbitration clause entered into by the debtor before the start of the insolvency proceeding remains binding on the trustee or receiver absent specific limitations in the arbitration agreement. Likewise, the trustee or receiver may enter into new agreements for arbitration during the course of the insolvency proceeding.

In domestic arbitration, article 207 of the DCBA is to be observed, which requires the stay of all pending actions until the second meeting of the creditors (except for urgent matters). In Swiss international arbitration the relevant procedural rules adopted for the proceeding will be guiding. It is suggested that arbitration proceedings in any event should allow for sufficient time for the trustee (or the respective creditors) to familiarise itself with the claim.

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### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

In general, the DCBA may allow a financially distressed company to seek rehabilitation under the protection of the court. Special rules apply to public entities, hotels, farms and some of the regulated businesses such as banks. Such a rehabilitation procedure is generally referred to as composition proceeding. Its most significant feature is that it is possible for the debtor, with the approval of the court, to force its creditors to conclude a settlement agreement and make it binding also on the dissenting creditors. The proceeding is designed to protect the debtor from enforcement proceedings (except the realisation of collateral for claims secured by a mortgage of real property) and to work out a suitable offer for a composition. During the proceeding the business of the debtor is generally operated under the supervision of a court-appointed

commissioner. The amended DCBA provides for the possibility of a debt moratorium to give the debtor time under protection of the court to rehabilitate without a composition agreement involving a haircut of the claims being intended. Upon order of the court such debt moratorium, which may not exceed four months, no public notification may occur. In such an event, a commissioner needs to be appointed to protect third-party interests.

Any composition agreement can only be confirmed by the court upon approval of either the majority of the admitted creditors representing two-thirds of the qualifying claims, or of one-quarter of the creditors with at least three-quarters of the total amount of the qualifying claims.

It is essential to realise that the composition agreement is designed to affect the non-secured (including the portion of secured claims that remains uncovered) and non-priority creditors only and thus it does not encompass a full reorganisation plan involving all creditors' claims. The types of composition agreements fall into the following categories.

#### **Moratorium**

The debtor is seeking a deferment of maturity of its obligation but promises to satisfy all creditors in full. This form of agreement could lead to a forfeiture of interest payment as, with the granting of the moratorium, interest ceases to accrue for all unsecured claims, unless the proposal specifically stipulates a claim on interest.

#### **Dividend agreement**

The debtor requests to be discharged from a certain portion of its unsecured and non-priority liabilities by proposing to pay to creditors a specific percentage of their claim according to a payment schedule. The proposal must be appropriate in view of the debtor's means, which are established during the proceeding. It is also now required that the owners or shareholder provide an adequate contribution as determined by the court.

In both the moratorium agreement and the dividend agreement, all of the prioritised claims and of the claims resulting during the moratorium with the approval of the commissioner, must be secured, but for third-class claims a secured completion is no longer required.

#### **Composition agreement in liquidation proceedings**

This composition agreement leads to an assignment to the creditors of a part or all of the debtor's assets for purposes of their realisation. It is conducted by a special liquidation proceeding that is conceived as a mild version of a liquidation and should allow for a better result for the creditors than with a bankruptcy. As in the case of bankruptcy, the debtor remains the legal owner of the assets until they are realised and their proceeds can ultimately be distributed to the creditors in accordance with the creditors' claim schedule. The creditors act via the appointed liquidator and the elected creditors' committee and they obtain the right to dispose of the debtor's assets.

Such a right can also be granted to a third party for some or all of the assets. A consequence of a composition by assignment of assets is that the creditors waive that part of their claim that will not be satisfied by the proceeds received from the realisation of the assets. No certificate of shortfall will be issued. In addition to the general provisions governing the composition agreement, a number of special provisions apply.

The amended DCBA now clearly stipulates that creditors' claims may be satisfied by issuing shares in a newly formed rescue company or in the debtor company.

#### **Composition agreement in bankruptcy proceedings**

As the debtor remains the legal owner of the assets, it can still make a proposal for a composition agreement once the bankruptcy proceeding has begun. The bankruptcy administrator will then assume the tasks of the commissioner and evaluate the proposal. Until the decision by the court to adopt or reject the proposed composition agreement, the liquidation of the debtor's assets will be suspended and if the agreement is confirmed, the court will revoke the bankruptcy.

#### **Procedural phases of a composition**

Typically, any composition proceeding is divided into four phases:

- approval procedure, beginning with the filing for a moratorium or initiation of the composition proceeding and ending with the granting of the moratorium by the court;

- moratorium proceeding, dealing with the effects of the moratorium and ending with the approval by the creditors of the proposed composition agreement;
- confirmation proceeding, focusing on the requirements and the procedure to have the composition agreement approved by the court; and
- completion proceeding, dealing with the fulfilment of the composition agreement or its respective supervision. In the case of an assignment of the assets, this phase involves the actual liquidation of assets and distribution of proceeds to the creditors.

#### **Releases in favour of third parties**

By operation of law, third parties and joint obligors will not be released because of the composition agreement with the debtor. To preserve such rights against third parties, certain procedural requirements must be observed, however (article 303 of the DCBA). The result of a dividend agreement (as opposed to a composition agreement with liquidation or bankruptcy) is that the creditors are prevented from pursuing officers' and directors' or other third-party liability claims, but such right would remain with the damaged debtor company. In the event of liquidation the right to pursue remedy for officers' and directors' liability (including claims against advisers or lenders when they have acted as factual corporate body) will be with the liquidator or bankruptcy administration. If the estate decides not to pursue such claims, the creditors are entitled to have this right assigned to them.

#### **Expedited reorganisations**

##### **24 Do procedures exist for expedited reorganisations?**

Under Swiss law, no specific procedures exist for expedited reorganisations. The moratorium period and the proceeding can be considerably reduced on the basis of a prior consensus with the creditors. In more substantial cases, it is not unusual that advisers discuss pre-petition with the court. The amended DCBA now favours a pure debt moratorium for a period of up to four months to rehabilitate financially distressed companies.

#### **Unsuccessful reorganisations**

##### **25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

The following can cause failure of a reorganisation plan:

- a strong minority of creditors disapproves the reorganisation and is in a position to preclude the double majority requirement from being met;
- the assets are insufficient to fully cover the privileged creditors and the claims incurred by the commissioner or administrator;
- the corporation is unable to do business during the moratorium period because of loss of reputation and lack of business;
- it becomes obvious to the court that the intended rehabilitation will not be achieved; or
- the debtor acts against the instructions of the commissioner.

An insolvent corporation that is no longer capable of reorganisation becomes bankrupt. If the plan is rejected the court will declare bankruptcy. If the composition agreement is not fulfilled with regard to a specific creditor, the latter may apply to the composition court to have the agreement revoked as far as its claim is concerned, without prejudice to its rights.

In a dividend (or percentage) composition, a creditor who has not received its dividend may request the revocation of the composition for its claim only and may demand full payment.

Finally, each creditor may apply to the composition court to revoke an agreement obtained by dishonest means.

## Insolvency processes

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

The opening of the bankruptcy is publicly announced by the bankruptcy office as soon as it has been determined whether ordinary or summary proceedings will be adopted. The announcement contains:

- personal information on the debtor and the time of the declaration of bankruptcy;
- the enjoinder to creditors of the debtor and all persons having claims to assets in the debtor's possession to file such claims with the bankruptcy office within one month of the announcement (including means of evidence);
- the enjoinder to debtors of the bankrupt to report to the bankruptcy office within the same period, subject to penal law consequences in case of non-compliance;
- the enjoinder to persons in possession of items belonging to the debtor, as holders of security rights or for other reasons, to deliver such items to the bankruptcy office; and
- the invitation to attend the first creditors' meeting, which takes place 20 days, at the latest, after the publication.

The first creditors' meeting makes the first decisions relating to the liquidation and the option of appointing a creditors' committee that will supervise the administration of the bankruptcy.

In the first creditors' meeting the bankruptcy officer has to provide a report on the inventory and on the bankrupt estate.

A second creditors' meeting is held after the claims are established in the creditors' schedule. Upon presentation of the administrator's report, it decides the further course of the proceedings. The report includes a comprehensive presentation of the assets, the creditors' claims and the status of the proceedings. Additional creditors' meetings will be called upon motion of one-quarter of the creditors, or of the creditors' committee or at the discretion of the bankruptcy officer. A final comprehensive report has to be submitted to the court by the bankruptcy officer upon close of the proceeding.

The reporting obligations of the insolvency administrator include a comprehensive report on the financial situation of the debtor on the occasion of the creditors' meeting and a report to the court as to the approval of the proposed composition agreement. In addition, annual status reports have to be submitted to the court by the liquidator in cases where the liquidation exceeds one year. Such report has to be pre-approved by the creditors' committee. In addition, a conclusive final report must be prepared and be approved by the court.

During the liquidation, additional reports will often be provided by the insolvency administrator to the creditors.

For a liquidation proceeding pursuant to a composition agreement with assignment of assets, in essence, similar rules apply. For the role of a creditors' committee usually appointed in such proceeding see question 28.

A creditor may pursue a remedy of the estate against third parties if the insolvency administrator with the support of the majority of the admitted creditors decided not to pursue the claim and the creditor has requested the assignment of the rights of the bankrupt estate. For the distribution of the fruits of such remedies see question 27.

Swiss law provides that a creditor agreeing to a composition agreement shall inform co-debtors and guarantors about place and date of the creditors' meeting and shall offer to assign them the creditors' claim against cash payment. If a creditor refrains from doing so aforementioned third parties are released of their liabilities. Furthermore, on a contractual basis a condition may be included in the composition agreement according to which the composition agreement is only concluded if certain third parties are also released from their liabilities.

## Enforcement of estate's rights

**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

If the bankrupt estate lacks sufficient free assets to conduct the bankruptcy proceeding, the proceeding will be terminated unless the necessary funds are provided by the creditors (DCBA, article 230). If the insolvency administrator with the support of the majority of the admitted creditors decides not to pursue a claim, each creditor is entitled to request the assignment of rights of the bankrupt estate to pursue. After deduction of the costs, the proceeds are used to satisfy the claims of those creditors who have pursued the claim relative to their amounts and ranking.

## Creditor representation

**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

With the amended DCBA the legislator has now introduced the opportunity of appointing a creditors' committee during the definitive debt moratorium. The commissioner must report to the creditors' committee, which has supervisory authority. In particular, the creditors' committee will authorise transactions during the debt moratorium involving the sale or charge of fixed assets, the provision of security or transactions without receiving consideration.

In the event of bankruptcy the creditors' committee is appointed at the first creditors' meeting. In the case of a composition agreement with liquidation the appointment takes place at the creditors' meeting approving the composition agreement. The election is done with a head count of the claims, each creditor having one vote only, irrespective of the magnitude of the claim and whether the claim is prioritised or not. One-quarter of the known creditors must be present to qualify.

In the case of a composition agreement the head count applies as well, but it is disputed whether the same qualifications apply as for the approval of the composition agreement or the requirements as they apply in a bankruptcy.

In a bankruptcy situation the creditors' committee is composed of three to five creditors or their (legal) representatives and ensures the interests of all creditors are preserved. The committee has no executive power but its decisions have to be implemented by the bankruptcy administration. The creditors' committee regularly has the following tasks:

- to supervise the activities of the bankruptcy administration, to address questions submitted and to object to any measures that contravene the creditors' interest;
- to authorise that the debtor may continue to run its business or trade, and under what conditions;
- to approve bills and to authorise the continuation of court proceedings and the conclusion of settlements and arbitration agreements; and
- to object to claims in the bankruptcy that the administration has admitted.

In a composition agreement with liquidation of assets, the liquidator acts under the control and supervision of the creditors' committee. It deals with the tasks set forth under the bankruptcy regime (above) and is assigned additional responsibilities:

- complaints by creditors regarding the liquidation of assets can be brought before this supervisory authority;
- approval of the creditors' claims schedule;
- decisions on the timing and procedure of asset liquidation;
- renouncement to pursue contested or otherwise difficult claims;
- approval of the reports presented by the liquidator; and
- decision on payments of interim dividends.

Additional authority and tasks may be stipulated in the composition agreement.

Compensation of the members of the creditors' committee is made in accordance with the specific tariff and is subject to court approval. Advisers may be retained but it is uncertain whether the (modest) rates of the tariff apply.

## Insolvency of corporate groups

**29** In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Except for accounting rules applied in a group context, Swiss statutory law does not provide a formal legal framework for groups of companies. Swiss law assumes each legal entity acts on its own. Basically, each company is obliged to protect and pursue its own interests independently from the interest of the controlling party. So insolvency proceedings are conducted separately. There is no pooling of assets and liabilities for a corporate group. Consequently, assets may not be transferred from an administration in Switzerland to an administration abroad. Assets located in Switzerland can, however, be marshalled by the foreign administrator pursuant to the Swiss mini-bankruptcy proceeding (see question 47).

## Appeals

**30** What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

The main decision-makers involved in the enforcement of Swiss insolvency proceedings are the bankruptcy administrator, the creditors' meeting and/or its elected administrator/receiver as well as the creditors' committee, if appointed. In essence, their decisions are subject to a specific complaint before the court. Basically, court decisions in insolvency proceedings are restricted to specific procedural stages. This includes the opening, revocation, suspension and termination of a bankruptcy proceeding. Moreover, in the course of composition with creditors, the composition agreement is subject to approval by the composition court.

Especially the court's decision on the opening of a bankruptcy proceeding and the confirmation of a composition agreement are of considerable legal and practical relevance. In both instances an appeal can be filed to challenge the respective court's decisions.

Against a decision on the opening of a bankruptcy proceeding (granting or rejection of the request to open such proceeding), an objection according to Swiss Civil Procedure Code (CPC) and DCBA can be filed within 10 days of its notification. The parties may plead new facts provided that these had arisen before the decision of the lower court was rendered. The appellate court will only set aside the lower court's decision on the opening of a bankruptcy proceeding if the appellant can present prima facie evidence that he is solvent as well as documentary evidence that, in the meantime, the debt, including interest costs, has been discharged, or that the amount owed has been deposited with the upper court for account of the creditor, or that the creditor has waived the carrying out of bankruptcy proceedings. A further appeal to the Swiss Federal Tribunal is possible.

An objection against the decision of the composition court can also be made. It must be filed within 10 day of notification of the parties about the composition agreement. The creditor's right of appeal against the court's confirmation of the composition agreement requires that he did not agree to the composition agreement and that the appellant took part in the hearings before the composition court stating its objection to the composition agreement. Again, a further appeal to the Swiss Federal Tribunal is possible.

Provided that the appellant fulfills the statutory requirements, he does not have to obtain a permission to appeal, but has an 'automatic' right of appeal by operation of law.

The requirement to post a security (advance payment) to proceed with an appeal from a court order in an insolvency proceeding is governed by Federal Law (CPC/DCBA). Within such guidelines the court has certain discretionary authority. The provision to post security has become standard procedure.

## Claims

**31** How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Creditors must submit their claims to the debt collection and bankruptcy office within a month after the public announcement of the opening of the bankruptcy. If filed late, the claim will nonetheless be admitted prior to the closing of the bankruptcy proceedings. Once the deadline for filing has elapsed, the bankruptcy authority examines each claim filed and undertakes the necessary inquiries for their verification. It invites the debtor to comment on each claim. Within 60 days, the bankruptcy authority is expected to draw up the plan for the order of the creditors (creditors' schedule), a time limit that, in practice, is extended regularly. This creditors' schedule contains all claims retained, including a statement of charges where the assets comprise real property. The creditors' schedule also indicates which claims have been disallowed and why. As long as the creditors have constituted a creditors' committee, the creditors' schedule and the statement of charges are submitted to it for approval.

An appeal by a creditor is possible against the disallowance of its claim by instituting legal proceedings. This has to happen within 20 days of the announcement of the claims schedule. If the creditors have agreed to waive a claim against the debtor, the bankruptcy authority may authorise the transfer of the claim to any creditor who requests it. The assignee will act in its own name and at its own risk to recover the claim. Should a balance subsist after realisation, it will be proportionally distributed among the creditors according to the claims schedule.

With some minor exceptions stated in the DCBA that prohibit the transfer of specific claims, creditors are generally entitled to transfer claims. A partial assignment, however, may not be misused to change the original voting power allocated to a specific claim. In addition, contractual agreements may stipulate restrictions regarding assignment. The relevant creditor for the proceedings, including for distribution, is the duly registered creditor. Hence, any claim transfer should be notified to the bankruptcy officer or liquidator. As a consequence of the (notified) transfer, the transferee assumes the legal status of the creditor. Regardless if the transferee acquired a claim at a discount, the transferee may enforce the claim for its full face value.

Contingent claims (ie, those that have not materialised but are subject to a post-petition or bankruptcy opening event) will be fully recognised in a liquidation but the liquidation proceeds allocated to those claims may not be received by the creditor until the event has materialised. In the case of a composition agreement the court decides if and to what extent contingent liabilities shall be admitted. Claims for unliquidated amounts are admitted in the liquidation proceedings provided the cause of the claim is established prior to bankruptcy or beginning of the composition proceeding. The amount of the claim to be admitted is subject to the verification process described above. In the case of a composition agreement the court decides if and to what extent contingent liabilities or unliquidated amounts shall be admitted for purposes of voting on the composition agreement.

For a composition agreement with assignment of assets, similar rules apply as for bankruptcy. Claims already submitted for the preceding debt moratorium do not have to be refiled.

With regard to the interest, a creditor may, in principle, only claim for the interest which had accrued by the date of the opening of the bankruptcy proceedings. As an effect of the opening of bankruptcy proceedings, interest ceases to accrue against the debtor. However, an exception is made for claims secured by pledge. For these types of claims, interest continues to accrue until the realisation of the respective collateral, provided the proceeds exceed the amount of the claim and the interest which had accrued by the date of the opening of bankruptcy proceedings.

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### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The DCBA (and the CO in case of an absolute subordination) clearly defines the ranking of claims. In bankruptcy or liquidation proceedings the decision on the ranking of a claim is part of the adjudication process. Any creditor whose claim has been rejected in part or totally or was not allocated the rank requested can bring legal action against the bankrupt estate. Similarly, a creditor may challenge in court the admission of another creditor's claim (DCBA, article 250).

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### Priority claims

#### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

All creditors that dispose of claims against the bankrupt debtor are able to participate in the bankruptcy proceedings. No restrictions exist as to nationality, jurisdiction or territory, but secured creditors always enjoy priority over unsecured creditors.

Article 219 of the DCBA sets up three different classes of unsecured creditors for the distribution out of the proceeds of the entire remainder of the bankrupt estate:

- first class – unpaid claims of employees that arose or became due not more than the six months prior to the opening of bankruptcy proceedings, but not exceeding (currently) 126,000 Swiss francs, and claims arising from premature dissolution of the employment relationship because of the opening of bankruptcy proceedings against the employer and the restitution of deposited securities; insurance policyholders may avail themselves of their rights granted by the federal legislation and may enforce claims in connection with professional welfare institutions; outstanding pension plan contributions to be paid by the employer; claims for maintenance and assistance derived from family law that arose during the six months prior to the opening of bankruptcy proceedings and that are to be performed by payments of money;
- second class – unpaid social security contributions; certain claims of persons whose assets were entrusted to the debtor as holder of parental power; deposits with banks kept in the name of the depositor (or short-term bonds) up to 100,000 Swiss francs; and
- third class – all other claims.

It should be noted that taxes are not prioritised; the privilege for VAT claims was abolished as of 1 January 2014.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Employment contracts are not terminated for reason of opening a bankruptcy, liquidation or composition agreement, but essentially in accordance with the contractual termination terms. However, the employee can request early termination unless the payment of compensation for future services is adequately secured. In the case of a transfer of business (or part) the buyer can now decide whether it wants to continue the employment. Also, joint and several liability with the seller for employment claims is no longer enforced. The rules relating to mass dismissals no longer have to be observed in the case of a bankruptcy or composition proceeding. Generally, pensions plan schemes in Switzerland are operated independently of the employer's business. The pension fund enjoys first-class privilege for unpaid contributions.

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### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

The Swiss pension and social security system is operated by entities that are legally independent of employers. Claims under occupational pension schemes (second pillar) enjoy first-class priority, and claims of all the other social insurance institutions are satisfied in the second class.

The status of the occupational pension scheme does not only apply to outstanding premiums but to all claims by the scheme against the insolvent employer (eg, loan claims).

If an occupational pension scheme suffers a cover shortage and the employer becomes insolvent, the contract between occupational pension scheme and employer will be terminated. A cover shortage is given when the pension benefits of a pension scheme are no longer covered in full (100 per cent) by the pension scheme assets. In this case, the occupational pension scheme is obliged to conduct a partial liquidation and the cover shortage is proportionally passed on to the insured persons. However, such reductions are only permitted in non-mandatory occupational pension provision (pillar 2b).

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Swiss legislation on insolvency does not provide for specific environmental-related provisions. Pursuant to the Federal Environmental Protection Act of 7 October 1983 (EPA), which applies, in principle, also to insolvency proceedings, the operator of an establishment or an installation that represents a special risk to the environment is liable for the loss or damage arising from effects that occur when this risk is materialised (EPA, article 59a). This applies to parties who acquire the establishment or operation from an insolvent estate. A director, officer, liquidator or other person entrusted with the debtor company's management or liquidation may (indirectly) be held liable for damages caused to the debtor company or its creditors if he or she has intentionally or negligently acted in breach of his or her duties defined by environmental law. Subject to specific situations (eg, factual corporate bodies; see question 41), there is no mechanism that directly shifts liability to a secured or unsecured creditor or any other third party.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

The claims that form part of a reorganisation proceeding will be consummated by the payment plan and the composition agreement becomes binding on all creditors whose claims either arose before the granting of the moratorium or have arisen without the receiver's consent and all respective enforcement proceedings are terminated (DCBA, article 310).

If the composition agreement is not fulfilled, respective creditors may apply to the court to have the agreement revoked (DCBA, article 316).

Liabilities secured by mortgages on real estate and similar registered assets will be passed on to the purchaser.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

Upon receipt of the proceeds of the entire bankrupt estate and after the schedule of claims has become definitive, the bankruptcy administration prepares the distribution plan and the final account. All costs for the opening and carrying out of the bankruptcy proceedings and for the drawing up of the inventory are paid first, directly out of the proceeds. The distribution list and the final account are made available for inspection at the enforcement office for 10 days. Interim dividend payments can be made.

Secured creditors have a preferential right to be paid out of the proceeds of the realisation of their collateral. They participate as unsecured creditors to the extent of a shortfall of the collateral.

Each creditor receives a certificate of loss in respect of the unsatisfied amount of its claim. This is an official certification of the loss incurred by the creditor, which allows the creditor to initiate new proceedings against the debtor subsequently.

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**Transactions that may be annulled**


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**39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

It is explicitly provided that the bankrupt estate includes everything that can be the subject of an avoidance action (similar rules exist for individual enforcement proceedings). Certain transactions that were concluded pre-bankruptcy can be challenged and set aside by the court with the effect that specific assets of the debtor will be referred to the estate and the creditor is left with the claim he or she had prior to receiving the consideration now restituted.

Three different types of transactions are voidable:

- gifts and equivalent transactions;
- transactions concluded in an over-indebted situation such as the provision of security for an unsecured debt without prior respective obligations, the satisfaction of a money claim other than by usual methods of payment, and the payment of claims which are not yet due. The transaction will not be set aside if the beneficiary can demonstrate that it did not know about the critical financial status of the debtor and was not bound to know; and
- transactions concluded that are knowingly disadvantageous to creditors in general, or for the benefit of individual creditors (fraudulent conveyance).

A considerable number of court decisions have been delivered supporting clawback claims. As a result, lenders' risks have substantially increased for pre-petition transactions. The same rules apply for a composition agreement in liquidation proceedings. In the case of a reorganisation the court may consider the impact and remedy of illicit transactions when asked to approve the composition agreement. See question 42 for special procedural rules that apply to transactions with closely related persons. Transactions that occurred during the debt moratorium may no longer be challenged if approved by the creditors' committee or the court.

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**Proceedings to annul transactions**


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**40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

The suspect period for gifts and equivalent transactions and for qualified transactions concluded during the status of over-indebtedness starts one year before the declaration of bankruptcy and five years in the case of fraudulent conveyance (the suspect period does not count preceding term of a moratorium or time used for a preceding debt collection).

Voidable transactions can first be attacked by the bankruptcy administrator or liquidator, respectively. However, if the creditors decide that the estate should not pursue the claim, each individual creditor (secured or unsecured) can request that the right to pursue the claim be assigned to him. Where there are several assignees, they have to proceed jointly. If successful, the assignee (and the co-plaintiffs) will enjoy the benefit but they also have to bear the litigation costs if the case is lost. The prescription period to bring legal action is two years from the date of bankruptcy or confirmation of the composition agreement with assignment of assets, as applicable.

Because the avoidance action is considered an enforcement remedy for which only the local courts have jurisdiction, the recognition and enforcement of a respective judgment will not fall within the scope of the Lugano Convention.

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**Directors and officers**


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**41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

For legal entities in general, their liabilities have to be satisfied by their own assets. The personal liability of corporate officers and directors arises in the context of a violation of their duties of responsibilities. This also applies to government claims, in particular personal exposure

can result in the context of non-payment of social security or withholding tax.

Article 754 of the Code of Obligations provides that any member of the board of directors or any person entrusted with management or liquidation is liable for any damage caused to the corporation, its shareholders or creditors where he or she has intentionally or negligently acted in breach of his duties. This responsibility does not apply only to the formally appointed representatives but also to what are termed 'factual corporate bodies' (all those persons who in reality decisively influence the corporate decision-making process). The principles of fiduciary duties are specified in a number of statutory provisions that aim at the protection of the shareholders as well as of the creditors' interests. Further specifications are laid down in the company's by-laws and organisational rules.

Of particular interest is the provision of article 725 of the Code of Obligations (see question 13). Lastly, the Swiss Penal Code sanctions reckless bankruptcy or mismanagement.

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**Groups of companies**


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**42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

Neither Swiss corporate or insolvency law provides for a formal legal framework for groups of companies. Swiss law assumes that each legal entity acts on its own. Basically, each company is obliged to protect and pursue its own interests independently of the interest of the controlling party and, in principle, the shareholder's duty is limited to paying the share capital that has been subscribed. A parent or affiliated corporation or natural person may, however, become responsible for the liabilities of a subsidiary if undue influence on the decision-making process of the subsidiary is exerted and the position of the material or factual corporate body is assumed. Often, contractual undertakings are entered into such as primary or accessory guarantees, undertakings as direct co-obligor or letters of responsibility. Case law has developed for parental liability on the basis of justified reliance by third parties on the business conduct of the parent company supporting the subsidiary. On fairly rare occasions the piercing of the corporate veil doctrine is applied, when it is considered abusive to claim the legal independence of a company. In such abusive, rare cases a court may decide to order a distribution of group company assets without regard to the assets of the individual corporate entities involved.

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**Insider claims**


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**43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

See questions 39 and 40 for the general rules on clawback claims. The amended DCBA, in sections 286, paragraph 3 and 288, paragraph 2 have changed the burden of proof for closely related persons, such as directors of the board, controlling shareholders and other closely related persons, including, in particular, group companies. They (and not the claimant) must prove that the respective transaction was at arm's length or that there was no intent to harm other creditors.

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**Creditors' enforcement**


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**44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

Apart from the ordinary liquidation procedure that may be requested by shareholders, it is possible to liquidate a business outside the bankruptcy process by merger, demerger and transfer of assets and liabilities. This is specifically provided for by the Merger Act, which came into force on 1 July 2004. Full creditor protection is required in such a process.

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**Corporate procedures**


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**45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

According to articles 736 to 751 of the Code of Obligations, a corporation is capable of being subject to an ordinary dissolution or liquidation

### Update and trends

The 'too big to fail' issue still influences Swiss insolvency law. In September 2015, PostFinance, a publicly owned subsidiary of Swiss Post, was added as number five to the list of systemically important banks.

A revision of Swiss company law is planned that (among other things) shall include an additional early warning system according to which members of the board of directors are required to prepare a cash flow forecast for the next 12 months that needs to be reviewed by a licensed auditor if there is reasonable doubt that the company remains solvent over the next 12 months or if the income statements of three consecutive years show a loss. This is a strong signal that pre-insolvency restructuring proceedings are further on the rise in Switzerland. However, the aforementioned revision is only proposed and is still in the stage of parliamentary deliberation. It remains uncertain if and when this revision will come into force.

The recognition of foreign bankruptcy and like orders shall be modernised in the future. By mid-October 2015 the Swiss Federal Council released a legislative proposal to change the current law (see question 47). In short, it is planned that the recognition proceeding shall be simplified and international cooperation enhanced. Reciprocal treatment by the requesting state shall no longer be needed and the

Swiss 'mini-bankruptcy' (ie, ancillary proceeding for assets located in Switzerland) may not have to be initiated at all if there are no domestic creditors to be protected. If an ancillary proceeding in Switzerland is found not to be necessary for the collection of the assets in Switzerland the foreign bankruptcy administrator may act with the same authority previously given to the debtor. In addition, bankruptcy (and like) orders shall in future be recognised if rendered by the competent authorities at the debtor's centre of main interest (COMI). The proposal is at the stage of legislative consultation.

The Swiss Federal Council intends to impede the abuse of the bankruptcy proceedings by amending the DCBA. To this end, in particular, the costs of bankruptcy proceedings shall be passed on to the debtor. Furthermore, measures shall be introduced to stop businesses from continuing their business activities despite confirmed non-payment of public debts. This proposal is not yet approved.

Finally, the Swiss Federal Council aims to ensure free market access for professional party representatives in foreclosure proceedings. In order to meet this objective and to ensure that every person with capacity to act is eligible to represent parties in Swiss foreclosure proceedings, legislative powers of the cantons shall be withdrawn. This proposal has not yet been approved.

procedure that involves no intervention by the judge or creditors. In that event, the board of directors or the liquidator is in charge of the liquidation.

Liquidators are appointed by the shareholders or by the court where the dissolution of the corporation is judicially ordered. The duties of the liquidators include the establishment of a balance sheet and of the information regarding the creditors of the dissolution. The liquidators terminate all current business before distributing the corporate assets, or the proceeds thereof, among the shareholders and give notice to the commercial register that the corporation has been dissolved.

Creditors' claims must be satisfied in full before this. A blocking period of at least one year must be observed prior to the payment of the liquidation dividend. An early distribution after three months is possible upon certification by a qualified auditor that no creditor or possible third-party interests are jeopardised.

As opposed to bankruptcy proceedings, corporate liquidation is not subject to verification by the court.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

In the event of bankruptcy, closing judgment is given as soon as the liquidation is finished.

In the event of reorganisation, a report is submitted to the judge after the composition has been implemented.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

Switzerland is a signatory to the Lugano Convention on Jurisdiction and the Enforcement of Judgments in Civil and Commercial Matters 1988. In proceedings concerned with the enforcement of judgments, the courts of the contracting state in which the judgment has been or is to be enforced according to the Lugano Convention shall have exclusive jurisdiction. The revised Lugano Convention entered into force on 1 January 2011. The revised Lugano Convention aligns Switzerland with the EU system of jurisdiction and enforcement of judgments throughout Europe. With the revision, the territorial application of the convention has been enlarged to include the new states of the European Union; significant changes relating to jurisdictional issues, exequatur proceedings and new provisions for provisional and protective

measures are adopted. In line with this, significant amendments were made to DCBA, for example, regarding freezing orders ('arrest').

If the debtor is domiciled in Switzerland and there are assets abroad, article 197(1) of the DCBA provides that all seizable assets owned by the debtor at the time of the opening of the bankruptcy proceedings, irrespective of where they are located, form one sole estate (the bankrupt estate). However, the extraterritorial effect of the Swiss bankrupt estate depends on whether and to what extent the foreign state where the assets are located recognises the Swiss bankruptcy decree. Therefore, the inclusion of foreign assets in the Swiss bankrupt estate is only possible if the foreign authorities are obliged to recognise the Swiss bankruptcy decree (as is the case in Germany, for example).

If the debtor is domiciled abroad and part of his assets are located in Switzerland, the PILA has established basic rules for the recognition in Switzerland of foreign bankruptcy decrees or orders for a composition with creditors or similar proceedings. Based on this law, the foreign main proceeding can be recognised, provided that the following prerequisites are met:

- proper jurisdiction of the foreign court;
- enforceability;
- observation of minimal due process standards;
- reciprocity; and
- no violation of Swiss public policy.

To receive recognition, the request must be brought before the court at the location of the assets in Switzerland. If successful, the recognition of the foreign decree subjects the debtor's assets in Switzerland to the consequences of Swiss law (the DCBA) in what is referred to as a 'mini-bankruptcy' proceeding. Such proceeding neither provides for a creditors' meeting nor a supervisory committee. The (Swiss) schedule of claims only includes secured creditors and unsecured privileged creditors domiciled in Switzerland. After distribution of the proceeds according to the (Swiss) schedule of claims, any balance must be remitted to the foreign bankruptcy estate or to those creditors who are entitled to it. However, such balance will only be remitted after recognition of the foreign schedule of claims by the Swiss court. The Swiss court will examine whether the ordinary (ie, unsecured and not privileged) claims of Swiss creditors have been properly admitted in the foreign (main) proceeding. With certain restrictions, Swiss assets can thus be marshalled for the main foreign proceeding.

Alternatively, if the debtor is domiciled abroad but runs a business operation in Switzerland, the 'branch bankruptcy' according to article 166(2) of the PILA and article 50 of the DCBA must be followed. The local and foreign creditors of the Swiss business operation (but only to the extent that such claims derive from operations of such branch office) can enforce their respective claims against the debtor's assets located in Switzerland, which can lead to a specific branch bankruptcy proceeding.

Also, debtors domiciled abroad may elect special domicile in Switzerland for the performance of an obligation with the consequence

that they become subject to Swiss enforcement for that obligation (DCBA, article 50(2)).

Another possibility is a freezing order according to article 271 of the DCBA. Such a freezing order, however, would cease to apply once the foreign bankruptcy administration or another bankruptcy creditor successfully requests the opening of a mini-bankruptcy proceeding.

In a more recent court decision, the adoption of the UNCITRAL Model Law by Japan helped to overcome the denial, so far, by Swiss courts to recognise reciprocity. It could be evidenced that the previous strictly followed principle of territoriality was given up by Japan permitting the Swiss court to acknowledge reciprocity. Hence, reciprocity between Switzerland and Japan for bankruptcy orders should by now be established. (See Update and trends.)

In the case of an insolvency of a foreign bank with assets in Switzerland, FINMA has far-reaching authority to recognise the foreign decree and to possibly cooperate with the foreign administrator (see 'Update and trends').

## COMI

### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

In Switzerland, debt enforcement and bankruptcy proceedings can exclusively be initiated and take place at the registered seat of a debtor company as reflected in the commercial register. In contrast to the European Regulation on insolvency proceedings, which is based on the principle of COMI (EC 1346/2000, article 3), Swiss law focuses on the formal criterion of the registered seat according to the theory of incorporation. As a consequence of these different approaches, Swiss courts may refuse to recognise a foreign insolvency decree rendered by a court at the COMI of the debtor because of a lack of competence (from the point of view of Swiss law) of the foreign court (PILA, article 166). See question 49 for cases dealt with by FINMA.

(See Update and trends.)

## Cross-border cooperation

### 49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

The Swiss legal system provides for recognition of foreign insolvency proceedings pursuant to the rules of the 'mini-bankruptcy' proceeding

(PILA, articles 166 to 175; see question 47). Swiss legislation does not specifically address international cooperation court to court or between domestic and foreign insolvency administrators. In the course of a Swiss mini-bankruptcy (a secondary proceeding) coordination is to a certain degree formalised. On an informal basis certain exchange of information court to court may be arranged on a case-by-case basis. Once the insolvency proceeding is opened the insolvency administrator will handle the proceeding. A Swiss administrator has to marshal the assets worldwide; his authority abroad will be determined by the law of the country concerned. On that level, pragmatic solutions are often sought. Applications for recognition of foreign insolvency orders can be frustrated because of a lack of recognition of reciprocity or for the reason that the insolvency ordered for which recognition is sought is not rendered by the court of the registered office of the corporate debtor (see question 48). FINMA acts in court capacity with regard to institutions regulated under the SFBA. FINMA may recognise an insolvency order issued by the court of actual (instead of registered) domicile of the debtor FINMA. BIO-FINMA requires that actions taken shall be coordinated with foreign authorities.

Some historic international bankruptcy treaties that were entered into by certain (but not all) Swiss cantons also need to be consulted to see whether different rules of cross-border cooperation applies:

- Bankruptcy Treaty of 12 December 1825 and 13 May 1826 with the (former) Kingdom of Württemberg;
- Treaty with the (former) Kingdom of Bavaria of 11 May and 27 June 1834; and
- Treaty with the (former) Kingdom of Saxony of 4 and 18 February 1837 (see 'Update and trends').

## Cross-border insolvency protocols and joint court hearings

### 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

Cross-border protocols are increasingly used in international insolvency cases.

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# Thailand

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

In Thailand, the Bankruptcy Act BE 2483 (AD 1940) as amended (the BA) is the law governing bankruptcy matters. In the BA, there are also sections that directly deal with reorganisation matters. Bankruptcy and reorganisation procedural matters are stipulated in the BA; the Establishment of and Procedures for Bankruptcy Court Act BE 2542 (AD 1999) (EPB); and Regulations for Bankruptcy Cases BE 2549 (AD 2006). The test of insolvency is mainly whether a debtor has debt greater than his or her assets. In addition, under the BA, there are presumptions as to whether a debtor is insolvent.

## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The Central Bankruptcy Court, Regional Bankruptcy Court and Supreme Court, Bankruptcy Division, are the specialised courts that have jurisdiction to adjudicate bankruptcy and reorganisation matters.

In bankruptcy and reorganisation proceedings, there are two levels of court. On the first level, the Central Bankruptcy Court and Regional Bankruptcy Court are the courts of first instance. Any appeal of either the judgment or order (or both) thereof can be made directly to the Supreme Court, Bankruptcy Division.

## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

According to section 7 of the BA, the Thai court of jurisdiction may order that an insolvent debtor be declared bankrupt if such debtor is domiciled in Thailand or operates its business in Thailand within one year prior to the date that such debtor files for bankruptcy. In addition, section 9 of the BA specifies that an entity can file for bankruptcy if certain conditions are met. The requirements for an entity to file for bankruptcy are mainly the same except that a juristic person is required to have indebtedness with one or more creditors of not less than 2 million baht in total. Therefore, an entity, including a foreign entity, who meets the above requirements, may be declared bankrupt by the Thai court.

Currently in reorganisation proceedings, only a debtor who is a limited company or public limited company can file for or be subject to involuntary reorganisation under the BA in accordance with the definition of debtor under section 90/1 of the BA. However, section 90/1 also opens the process to other juristic persons included in ministerial regulations. An interesting example is Credit Union Co-operative which is included in the definition of 'debtor' in the Ministerial Regulation of the Ministry of Justice dated 5 August 2014 (published in the Government Gazette on 7 August 2014). Consequently, the Credit Union Co-operative entered into reorganisation proceedings and is now in the reorganisation plan process.

Excluded assets from insolvency proceedings are personal and necessary effects that the debtor, his or her spouse and his or her minor

children reasonably require in accordance with their condition in life; and livestock, seeds, instruments and items for use in the debtor's occupation, of a total value not exceeding 100,000 baht.

## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There is no specific procedure in respect of the insolvency of a government-owned enterprise. If a government-owned enterprise enters into insolvency proceedings, they shall follow the same procedure as a private enterprise.

There is no special remedy for creditors of an insolvent public enterprise. Such creditor shall enjoy the same remedies as a private enterprise.

## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

Currently, there is no legislation enacted specifically to deal with the financial difficulties of institutions that are considered 'too big to fail'. However, under the Financial Institution Business Act, prior to entering into reorganisation proceedings in respect of a debtor that is a commercial bank, a finance company or a credit foncier company, the Bank of Thailand may take control over the said financial institutions. As such, the directors, officers and employees of the financial institutions will be prohibited from conducting further business of that financial institution unless authorised by the control committee. The control committee has the duty to undertake all business of the financial institution placed under control, including having the financial institution merged with or transferred to another financial institution when deemed appropriate. A similar control mechanism is applicable to insurance companies and security companies under the Life Insurance Act, Non-Life Insurance Act and Securities and Exchange Act.

## Secured lending and credit (immoveables)

### 6 What principal types of security are taken on immoveable (real) property?

Under Thai law, an immoveable (real) property can be taken as security by way of mortgage under the Civil and Commercial Code (the CCC), and security under the Business Security Act BE 2015 (the BSA). This year Thailand has launched new legislation, the BSA, which came into force on 2 July 2016. The BSA makes significant changes to the regime for creating security in Thailand by, among other things, expanding the types of assets that Thai entities can use as security for their financing, and establishes a new method of creating security; the business security agreement.

Depending on the type of mortgage, security can be in the form of:

- immoveable property such as lands and buildings;
- certain moveable assets (ie, ships of five tonnes and over, floating houses, beasts of burden); and
- any other moveable properties with regard to which the law may provide registration for that purpose such as machinery that is registered with the Central Office for Machinery Registration,

the Department of Industry in Thailand under the Machine Registration Act BE 2530, or any moveable assets that can be mortgaged under a specific law.

For example, ships of 60 tonnes gross or over for the purpose of a sea voyage can be mortgaged under the Mortgage of Ships and Maritime Lien Act BE 2537.

Under the CCC, a mortgage must be made in writing and registered with the competent authority. The CCC also prescribes certain details that must be specified in the mortgage agreement; for example, the mortgaged amount is required to be in Thai baht (except for ships mortgaged pursuant to the Mortgage of Ships and Maritime Lien Act BE 2537 where the mortgaged amount can be in foreign currency) and the details of the secured obligations. A title document in respect of mortgaged property is not required to be delivered to the mortgagee in order to perfect a Thai law mortgage. However, in practice, the original land title deeds of mortgaged property are usually required to be in the possession of the mortgagee throughout the term of the mortgage agreement.

It is important to mention that the same asset may be subject to several mortgages in favour of several mortgagees (which have different rankings depending on the time of registration of the mortgage); the first registration of the mortgage is considered as the first in priority, and the first mortgagee will be entitled to first receiving debts payment in priority over the second or other mortgagee. The creditor who accepts the mortgage is regarded as a secured creditor under the Thai bankruptcy proceedings under the BA.

Apart from mortgage, immovable property can be taken as security by way of security under the BSA; see further details in question 7. It is worth noting that the land that can be used as security by way of a business security agreement under the BSA is only the land on which the security provider operates the business of immovable property directly and the security receiver must be a financial institution or any other person to be prescribed in a ministerial regulation. At present, since the BSA is very new, we understand that there is no precedent involving a financial institution taking the land of the security provider who operates the business of immovable property as a security under the BSA.

## Secured lending and credit (moveables)

### 7 What principal types of security are taken on moveable (personal) property?

Under section 6 of the BA, a secured creditor means 'the creditor holding rights over the asset of the debtor in a mortgage, pledge or a right of retention, or a creditor possessing preferential rights in the nature of a pledgee.' Practically, the pledge and the right of retention are currently the principal types of security taken on moveable (personal) property. It is vital to note that a creditor holding rights over the asset of the third person or holding any other kind of security of a third person is not recognised as a secured creditor under the bankruptcy proceedings. However, such creditor still has the right to enforce such security under the civil procedure.

In general practice, a pledge under the CCC can be taken as security over the following moveable properties and the following perfections are required to be carried out.

#### Moveable property (eg, machinery or automobile)

The perfection of the pledge over moveable property or rights with respect to a moveable property requires the delivery of the pledged property to the pledgee or to a third person acting on behalf of the pledgee. As Thai law requires the possession of the pledged property by the pledgee throughout the term of the pledge in order to maintain the valid pledge, the pledge over moveable property which is still used in the business of the pledgor (for example, machinery) is not practical.

#### Right represented by a written instrument (eg, a bill of exchange)

The perfection of the pledge over a right represented by a written instrument requires the delivery of such instrument to the pledgee and the pledge being notified in writing to the relevant obligor. The pledge cannot be set up against third parties unless its creation is endorsed upon the instrument.

#### Shares in script/certificate form

The perfection of the pledge over shares (in scripted form) requires:

- delivery of the share certificate to the pledgee or to a third person acting on behalf of the pledgee;
- notice of the pledge to be delivered to the registrar of the issuing company; and
- the pledge to be recorded in the register of shares of the issuing company.

In the case of a listed company, the registrar of the shares is the Thailand Securities Depository Co, Ltd (the TSD). The parties must notify and register the pledge with the TSD by submitting an application together with required documents to the TSD.

Under Thai law, the pledge over the above assets is not required to be made in writing or in any special form. However, it is common to have a pledge agreement in writing signed by the parties.

#### Collateral over deposited securities

The collateral over deposited securities under the Securities and Exchange Act BE 2535 (the SE Act) can be taken as security over the securities deposited with the Stock Exchange of Thailand (which are in the scripless form). Securities under the SE Act are, for example, shares and investment units of a mutual fund. Generally, the perfection of this is that the parties must notify and register the security with the TSD by submitting an application together with required documents to the TSD.

Under Thai law, the collateral over deposited securities is not required to be made in writing or in any special form. However, it is common to have a collateral agreement between parties.

Note that the creditor who accepts the collateral over deposited securities shall have preferential rights in such securities in a manner similar to the pledgee, and, therefore, such creditor will also be regarded as a secured creditor under the Thai bankruptcy proceedings under the BA.

#### Security under the BSA

Under the BSA, security may be created over certain assets under a business security agreement, such assets are:

- a business;
- a right of claim (which includes a right to receive performance of obligations and any other rights, but excludes a right represented by a written instrument);
- moveable property used in a business such as machinery or inventory;
- immovable property used in a business;
- intellectual property; and
- other assets to be prescribed by a ministerial regulation.

A business security agreement must be made in writing and registered online with the Business Security Registration Office. The BSA also prescribes certain details that must be specified in the business security agreement; for example, enforcement events and the debt secured. In the case of a business security agreement over a business, the security receiver must file the consent of the security enforcer when registering the agreement.

It is important to note that the security receiver must be a financial institution or any other person to be prescribed in a ministerial regulation. A creditor that accepts a business security agreement is regarded as a secured creditor under Thai bankruptcy proceedings.

In relation to the priority established, this is similar to a mortgage. That is to say, the same asset may be subject to several business security agreements in favour of several security receivers (which have different rankings depending on the time of registration of the business security agreement); the security receiver who is registered first shall be entitled to receive debts payment before the security receiver who is registered thereafter.

If any asset that is already used as security under the BSA has also been mortgaged as a security to secure the debts, the rank of the security receiver and mortgagee shall be in the respective order of the day and time of registration, whereby the security receiver or mortgagee who is first registered shall be entitled to receive debt repayment before the security receiver or mortgagee who is registered thereafter.

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### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

In bankruptcy and reorganisation proceedings, since unsecured creditors do not have any right over the assets to be enforced for their sole benefit, the only means therefore available for unsecured creditors to obtain the repayment of debts lies with their rights to file an application for the repayment of debt. Subject to section 90/27 and section 91 of the BA, unsecured creditors are entitled to file an application for repayment of debt in both bankruptcy and reorganisation proceedings.

The procedure to prove the validity of such an application for the repayment of debt is not complicated. Still, the duration of these proceedings may vary depending on the case's complications and the availability of the court's docket. Practically, it would take up to three months for the official receiver to consider and make an order on the application for the repayment of debt.

There are measures provided under Thai law which prevent the debtor's transfer of assets. In bankruptcy proceedings, temporary receivership is available under section 17 of the BA and an interim injunction under section 254 of Civil Procedure Code is applicable *mutatis mutandis* by virtue of section 14 of the EPB prior to the rendering of the court's absolute receivership order.

With regard to the application for the repayment of debt, there is no special procedure applied to foreign creditors as Thai law does not differentiate the debt repayment application process between Thai and foreign creditors. In bankruptcy proceedings, a creditor in a foreign country can file an application for the repayment of debt within four months from the publication of an absolute receivership order while the creditor in Thailand is limited to a two-month period for filing the same application.

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### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

Thai law does not allow voluntary bankruptcy to be commenced by the debtor, except in the case that a liquidator of a dissolved debtor files a bankruptcy case where such dissolved debtor has insufficient assets to settle all debts.

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### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Under section 9 of the BA, a creditor is eligible to file for bankruptcy against a debtor.

To do so, the insolvent debtor must be proved to be indebted to one or more creditors in the amount of at least 1 million baht in total if an individual or indebted to one or more creditors in the amount of at least 2 million baht in total if an entity.

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### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

An insolvent debtor owing a definite amount not less than 10 million baht to one or more creditors is entitled to file a reorganisation petition in accordance with section 90/4 of the BA. Once the reorganisation petition is accepted by the court, certain activities involving the assets of the debtor will be subject to section 90/12 of the BA (see further details in question 15).

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### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

A single creditor, group of creditors, or the state agency authorised to supervise the business of the debtor as described in the BA, may file a reorganisation petition against the insolvent debtor if such insolvent debtor has a definite amount of debt of not less than 10 million baht. Once the reorganisation petition is accepted by the court,

certain activities involving the assets of the debtor will be subject to section 90/12 of the BA (see further details in question 15).

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

There is no Thai law that requires directors to commence bankruptcy and reorganisation proceedings. Nevertheless, the board of directors has a duty to call for an extraordinary general meeting of shareholders when the company is significantly at loss. If they fail to do so, each director may be held criminally liable with a penalty of up to 20,000 baht under the Act on Offences Concerning Registered Partnerships, Limited Partnerships, Limited Companies, Associations and Foundations BE 2499 (AD 1956).

Companies are not prohibited from carrying on business while insolvent. However, in a case where the creditor has known that the company (debtor) is insolvent at the time and yet still allows it to create debt, such debt (excluding debts which the creditor allowed to be created so that the debtor's business can continue operations) may not be claimed for repayment if insolvency proceedings are subsequently commenced.

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

The debtor is allowed to continue operating its normal business operation during a reorganisation pursuant to section 90/12(9) of the BA. However, the powers and duties of the debtor's executive in managing the business and assets shall cease once the court has ordered business reorganisation and the court may appoint any person(s) or the debtor's former executive to be an interim executive until the plan preparer is appointed. The debtor's assets cannot be sold except in the normal course of business unless such sale of assets is approved by the court. The debtor is allowed to make payment to creditors who supply goods or services according to normal and current terms and conditions of agreements. Any claims arising after the court's reorganisation order will not be subject to reorganisation proceedings, and if the debtor has incurred such obligations in the normal course of business and as required for the continuation of its operation, the debtor can pay such claims.

Creditors of debts created by the receiver or interim executive with a debt confirmation letter from a plan preparer and creditors of debts created by the plan preparer, plan administrator, interim plan administrator and receiver have the right to be repaid without having to file an application for repayment of debts for business reorganisation.

Under the BA, if the business reorganisation plan is successfully implemented and the court orders the termination of the reorganisation process, the debts of the creditors who supply goods and services after filing (created by the plan preparer, plan administrator, interim plan administrator, and receiver) will be treated as a first-rank privileged debt. In the event that the business reorganisation plan fails and the court orders the absolute receivership of the debtor, the debts of the creditors who supply goods and services after filing (created by the plan preparer, plan administrator, interim plan administrator, and receiver), will be treated at the rank of the expenses incurred by the receiver in the management of the assets of the debtor.

The creditors and the court have roles in supervising the debtor's business activities as the creditors are entitled to file a petition requesting the court to revoke any transaction in breach of section 90/12(9).

If the creditors approve the business reorganisation plan, they can be represented by a creditor committee to be selected at a creditors' meeting. The creditor committee will supervise the implementation of the plan by the plan administrator.

After the insolvency proceedings are commenced by or against the corporation, the directors and officers are not prohibited from exercising the powers in connection with the management of assets or business of the corporation. However, as prescribed by section 24 of the BA, once the court has ordered the debtor to be under receivership, the powers of the directors in connection with their corporation's asset or business will cease and are, by virtue of law, transferred to the official receivers. Pursuant to section 826 of the CCC, the powers of the officers empowered by the directors to act as their agent shall also terminate once the debtor becomes bankrupt. Nonetheless, the officers (agents) are obligated to take all necessary steps to protect the interests entrusted to them until the representatives of the principle can protect such interests.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

There are proceedings similar to a stay (automatic stay) as stipulated in section 90/12 of the BA. An automatic stay permits the debtor to continue to conduct business during the implementation of reorganisation proceedings by suspending existing lawsuits brought by creditors and prohibiting civil claims or actions to be filed against the debtor. Creditors may seek permission from the bankruptcy court to file claims.

The BA does not specifically provide for the application of an automatic stay in a bankruptcy case. The pending case involving assets of the debtor under bankruptcy proceedings may be suspended at the court's discretion.

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

In bankruptcy proceedings, when the court has ordered the debtor to go into receivership, the debtor is prohibited from carrying out any act relating to its assets or business, except those performed under the order or approval of the court, the official receiver, the administrator of the asset or of a creditors' meeting (as the case may be), as prescribed in the BA. Accordingly, the debtor is prohibited from incurring any additional debt, otherwise the transaction in breach will be void.

In reorganisation proceedings, the debtor is prohibited from undertaking certain activities during the term of automatic stay, such as incurring additional debt that is not done during the normal course of business, whether secured or unsecured. An automatic stay becomes effective on the date the court issues an order accepting the reorganisation petition.

### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

In bankruptcy proceedings, under section 102 of the BA, if a creditor who is entitled to claim for repayment of its debt is indebted to the debtor when the court issues the order placing the asset under receivership, even if the grounds for the debt of the two parties are not the same, or are subject to the conditions or terms, such debts may be offset against each other, unless the creditor's right of claim against the debtor accrued after the order of receivership of the asset.

In reorganisation proceedings, under section 90/33, if the creditor who is entitled to apply for repayment of debt for reorganisation is indebted to the debtor at the time of issuance of the reorganisation order, such creditor may exercise the right of set-off, unless the creditor acquires the claim against the debtor after the court issues a reorganisation order.

### Sale of assets

#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

In bankruptcy proceedings, under section 24 of the BA, after the rendering of the court's receivership order, the debtor is prohibited from engaging in any activity involving his assets, including sale of the assets. The official receiver is the only person permitted under the BA to sell the assets of the debtor. The sale of assets will be conducted through auction or other selling methods proved to be the most convenient and for the best interests of all creditors as stipulated in section 123 of the BA.

The claims and liabilities can be passed with assets depending on the terms and conditions of the sale.

In reorganisation proceedings, under section 90/12(9) of the BA, the debtor is also prohibited from selling the assets out of the ordinary course of business throughout the process, unless it is provided otherwise in the plan approved by the court. 'Stalking horse' bids and credit bidding are not specifically prescribed under Thai law.

### Intellectual property assets in insolvencies

#### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

There is no specific provision under the BA for the termination of IP usage or the extent of IP usage during the bankruptcy and reorganisation proceedings. Accordingly, the termination of IP usage or the extent of IP usage is governed by the terms of the agreement between the licensor and the licensee.

There is no provision under the BA prescribing the right to use the IP after the termination of the IP agreement.

### Personal data in insolvencies

#### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

There is no specific provision under the BA to restrict the use of personal information or the collection of customer data of the insolvent company. However, Thailand is currently drafting the Personal Information Protection Act. The draft is under the consideration of the National Legislative Assembly. Therefore, if such information is not recognised as a trade secret, it can be transferred.

### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

Under section 90/41-bis of the BA, only the plan administrator shall have the power to reject an unfavourable contract as specified in the reorganisation plan. The rejection right must be exercised within two months of the date on which the court approves the plan. Whoever suffers damages therefrom will have the right to file an objection with the court within 14 days of becoming aware of such rejection. If the court reaffirms the rejection, whoever suffers damages therefrom shall be entitled to apply for the repayment of debt for such damages under reorganisation proceedings.

Once the court issues an order accepting the petition for business reorganisation, section 90/12 of the BA prohibits the creditors from commencing a civil case in respect of the assets against the debtor if the obligation arises before the day on which the court approves the plan. If a breach of contract occurs, the creditors can choose to take action as follows:

- if the breach occurs before the court issued the order to reorganise the business, creditors can file an application for debt repayment with the official receiver;
- if the breach occurs after the day on which the court orders the reorganisation of business but before the day on which the court approves the rehabilitation plan, the creditors can ask the court for permission to take action against the debtor in a civil case; or
- if the breach occurs after the day on which the court approves the rehabilitation plan, the creditors can take action against the debtor in a civil case without having to seek permission from the court.

### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Bankruptcy and reorganisation proceedings will be initiated and proceed only in the courts, not in arbitration proceedings. No insolvency disputes are resolved by arbitration.

Under the BA, no creditors, including the creditors who initiate the bankruptcy of the debtor, can initiate a new bankruptcy case against the debtor in court after the court renders the absolute receivership order. In civil cases and arbitration proceedings, the BA does not specifically prohibit creditors from initiating these cases or proceedings. In practice, however, after the court renders the absolute receivership order on the debtor, the official receiver may ask the court or tribunal to dispose of the pending civil cases or arbitration proceedings.

In reorganisation proceedings, all actions against the debtor are put on stay and the creditors are prohibited from initiating arbitration or court proceedings against the debtor unless such prohibition is not necessary for the reorganisation proceedings.

The court cannot direct the parties to submit the dispute to arbitration.

### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

Under section 90/42 of the BA, the reorganisation plan must contain at least the following significant features: the reasons for reorganising the business; details of assets, liabilities and encumbrances; and principles and methods for reorganisation.

The reorganisation plan must be approved by resolution of the creditors' meeting. The BA provides a voting system whereby creditors are, according to section 90/42 bis, divided into the following groups or classes:

- secured creditors having a secured debt of not less than 15 per cent of the total debt for which a claim for repayment may be filed will be classed as one group. Other remaining secured creditors shall be classified in the same group;
- unsecured creditors may be classified in different groups. Unsecured creditors who hold the same or similar rights or benefits will be classified in the same group; and
- creditors that, under the law or contract, are entitled to receive payment only after other creditors have received payments in full.

The reorganisation plan must be approved by:

- special resolutions of the meetings of all groups of creditors; or
- a special resolution of the meeting of at least one group of creditors that is not a group of creditors that is deemed to have attended and voted to approve the reorganisation plan, provided that the aggregate amount of debt of creditors of all groups who voted to approve

the reorganisation plan constitutes not less than 50 per cent of the total debt held by creditors of all groups who attended the meetings in person or by proxies and voted at the respective meetings.

In addition, the creditors' approval of the reorganisation plan must be confirmed by the relevant court. The reorganisation plan confirmed by the court will bind both creditors that are not required to submit proofs of claims and those that must submit proofs of claims.

Practically, the reorganisation plan may contain the clause to release non-debtor parties from any liability arising out of the implementation of the plan. Nevertheless, any specification to limit the liability of non-debtor parties will not relieve them from the liability arising out of a wrongful act or gross negligence. Meanwhile, the reorganisation plan cannot release non-debtor parties from any liability arising prior to the reorganisation.

### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

There is no expedited reorganisation under Thai law but, in practice, the debtor can reduce the time-consuming nature of certain stages of the reorganisation by having major creditors agree on the principles of the reorganisation plan prior to the application for reorganisation.

### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

If the reorganisation plan is not approved by the creditors or is approved by the creditors but not confirmed by the court, the court will then cancel the reorganisation order. Upon a reorganisation cancellation order, the automatic stay will end and the powers and duties in managing the debtor's business and assets will devolve to the debtor's executive, but any acts done by the receiver, interim executive, plan preparer, plan administrator or interim plan administrator before such order will not be affected. The debtor's shareholders will also again enjoy their normal legal rights. Moreover, the receiver, interim executive, plan preparer, plan administrator or interim plan administrator, as the case may be, must hand over the assets, seals, accounting ledgers and documents relating to the assets and business operation to the debtor's executive promptly.

If the reorganisation is not successfully implemented in accordance with the reorganisation plan and the maximum period prescribed under the BA has elapsed, the court will either render an absolute receivership order if the court deems that the debtor should be declared bankrupt, or render an order to terminate the reorganisation.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

In bankruptcy proceedings, certain notices are to be given to creditors:

- notice to convene the first creditors' meeting;
- notice to convene the creditors' meeting for the composition prior to or after being declared bankrupt; and
- notice of the court hearing for the consideration of the composition.

Certain information will be available to creditors or creditors' committees, for example, details of the composition and details of the debtor's estate and business. The official receiver has the duty to report to the court on the administration of the debtor's assets and the conduct of the bankrupt person.

Under Thai law, the estate is included in the assets of the debtor. And only the official receiver is empowered by the BA to pursue the estate's remedies (rights to claim repayment or demand the delivery of an asset) against third parties.

Under the BA, only the liability of the debtor can be released under the reorganisation plan. In addition, according to section 90/60

paragraph 2, the liability of the guarantors or the joint-debtors of the debtor cannot be released under the reorganisation plan.

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

In bankruptcy proceedings, the official receiver is empowered by the BA to pursue the estate's remedies (rights to claim repayment or demand the delivery of an asset) against third parties.

In reorganisation proceedings, under section 90/38 of the BA, the planner, the plan administrator or the official receiver is entitled to submit a petition requesting the court to compel those persons, who admit that they are indebted to the debtor or have assets of the debtor in their possession, to pay the debt or turn over those assets. On the contrary, if such persons do not admit that they are indebted to the debtor or they have assets of the debtor in their possession, the planner or the plan administrator must notify the official receiver to proceed with any further actions in accordance with section 90/39 of the BA.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

In bankruptcy proceedings, under section 37 of the BA, the creditors' meeting may pass a resolution to appoint a committee of creditors in the matter relating to the management of the debtor's assets as prescribed in the BA.

In reorganisation proceedings, under section 90/55 of the BA, the creditors' meeting may pass a resolution to appoint a committee of creditors to act on behalf of all creditors in monitoring the implementation of the plan. In practice, the plan may specify that proper expenses be paid to the advisers of the creditors. There are cases where the court approved reorganisation plans which contained the payment of proper expenses to the advisers of the creditors.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

Under Thai law, there is no procedure for combining the parent company and its subsidiaries, thus, none of the assets and liabilities can be pooled for distribution purposes. The assets are not allowed under Thai law to be transferred from an administration in Thailand to an administration in a foreign country.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Pursuant to the Act on the Establishment of and Procedure for Bankruptcy, a judgment or order of the Bankruptcy Court in respect of a business rehabilitation cannot be appealed except if the judgment or order is for:

- dismissal of the plaint or dismissal of the petition or a petition asking for adjudication of bankruptcy;
- dismissal of the petition for business reorganisation;
- approval or disapproval of the repayment of debt;
- absolute receivership; or
- civil cases relating to bankruptcy proceedings.

Therefore, if the petitioner wants to appeal a judgment or order that is restricted to appeal, a petition must be filed to the Supreme Court asking for approval to appeal together with the statement of appeal. Where

the Supreme Court considers that the request is in the interests of justice, including if the order contradicts a previous judgment of another court or the Supreme Court, the Supreme Court will allow the appeal.

In addition, to appeal a judgment or order of the Bankruptcy Court, the petitioner must submit the appeal within one month of the date of judgment.

### Claims

#### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

In bankruptcy proceedings, in general, all creditors must file an application for the repayment of debt with the official receiver within two months of the date on which the court's order appointing the official receiver is published in the government gazette (the period may be extended at the official receiver's discretion, in the event such creditor is domiciled outside Thailand, for a period not exceeding two months). If a creditor fails to file an application for the repayment of debt, except for limited exceptions (ie, tax claims), such creditor will not be entitled to receive its share of the bankruptcy proceeds.

The official receiver shall submit the applications for debt repayment of all creditors along with his or her opinion for the consideration of the court and whether the creditors will be granted repayment of the debt is at the court's discretion. If the creditors wish to object to the court's order, they may appeal to the Supreme Court, Bankruptcy Division.

There is no specific provision under the BA that prescribes the transfer of claims. The transfer of claims is possible but subject to the discretion of the official receiver. The transfer of claims must be disclosed to the official receiver.

In reorganisation, all creditors must file an application for the repayment of debt within one month of the publication of the order for the appointment of the planner in the government gazette. If a creditor fails to file an application for the repayment of debt, it will not be entitled to receive payment under the plan and has no further recourse against the debtor, unless the reorganisation plan provides otherwise, or the court cancels the reorganisation order.

In reorganisation proceedings, the official receiver has a duty to approve the application for the repayment of debt, including the contingent or unliquidated amounts. Such contingent or unliquidated amounts will be determined by the official receiver based on evidence and the creditor's proof of claim. An interested person may appeal the decision of the official receiver for the consideration of the relevant court within 14 days.

In general, the transfer of claims in reorganisation proceedings is subject to the discretion of the official receiver or the court, depending on the stage of the consideration of the application for the repayment of debt.

Under Thai laws, a claim acquired at a discount can be enforced for its full face value.

In regard to interest calculation, in bankruptcy proceedings, interest incurred after the date on which the court orders receivership cannot be claimed pursuant to section 100 of the BA. In reorganisation proceedings, on the other hand, creditors are not prohibited from claiming interest incurred after the court orders the reorganisation of the debtor's business.

### Modifying creditors' rights

#### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

Under the BA, the court is unable to change the rank (priority) of a creditor's claim prescribed in the BA.

**Priority claims****33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

Under Thai law, secured debt has priority over unsecured debt. For unsecured debt, repayment will be distributed in the following order:

- expenses of administering the debtor's estate;
- expenses incurred by the receiver in managing the debtor's assets;
- funeral expenses of a deceased debtor appropriate to his status;
- fees incurred in collecting assets;
- fees of the petitioning creditor and counsel's fee, as the court or the receiver may prescribe;
- taxes which have become due for payment within the six months prior to the order for receivership; and
- other debts.

**Employment-related liabilities in restructurings****34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

Normal employee claims (eg, severance pay) will arise if the employment is terminated during the reorganisation proceeding. The procedure for termination during the reorganisation proceeding is then in accordance with Thai labour law. The number of employees being terminated during the reorganisation or the cessation of the business operation is not cause under Thai law for increasing claims. Also, the employee pension plan or scheme does not have any priority in the bankruptcy or reorganisation proceedings in Thailand.

**Pension claims****35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Under Thai law, there is no specific remedy for pension-related claims against employers in insolvency proceedings. Employees, along with other creditors, are required to file applications for the repayment of debt with the official receiver within two months of the date on which the court's order appointing the official receiver is published in the government gazette. This period of two months may be extended at the official receiver's discretion in the event that any creditors are domiciled outside Thailand for a period of up to two months. No priorities are attached to such claims.

**Environmental problems and liabilities****36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

Before the court orders the debtor to be under receivership, the directors are the persons responsible for controlling the environmental problem and for remediating the damage.

When the court has ordered the debtor to be under receivership, on the other hand, section 24 of the BA prohibits the debtor from taking action in relation to his or her assets or his or her business. Rather, pursuant to section 22 of the BA, the official receiver is entitled to do any necessary act to complete any pending business of the debtor. As such, if environmental problems, or any other circumstances in which the debtor is obligated by law to perform certain actions, occur, the official receiver has the authority to control the problem and to remediate the damage caused. The liabilities to compensate for the damages incurred will be imposed on the debtor.

**Liabilities that survive insolvency proceedings****37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

In bankruptcy proceedings, the liabilities of the debtor will survive in two cases: discharge from and termination of the bankruptcy.

In the case of discharge from the bankruptcy, there are two types of discharge: discharge from bankruptcy according to a court's order and discharge from bankruptcy after the lapse of a three-year period as prescribed in the BA. An order of discharge from bankruptcy will not relieve the debtor from debts related to tax or land tax and debts that have arisen through the dishonesty or fraud of the bankrupt, or debts for which creditors have not filed claims owing to dishonesty or fraud to which the bankrupt person is a party.

If the bankruptcy is terminated by the court because of the creditors' failure to cooperate with the official receiver, the debtor will not be adjudicated bankrupt and will not be relieved from its liabilities.

In reorganisation proceedings, the debts incurred prior to the rendering of the court's reorganisation order, which had been applied for, will be released after the implementation of the plan. After the rendering of the order to terminate the reorganisation, the debtor will be freed from all debt repayment that could be applied for in reorganisation proceedings. However, if the court revokes the reorganisation proceedings, all remaining debts that have not yet been repaid will remain.

**Distributions****38 How and when are distributions made to creditors in liquidations and reorganisations?**

In bankruptcy proceedings, once the assets of the debtor are sold, the distribution will be made to the creditors who have been granted the court's final order to receive the repayment of debt.

In reorganisation proceedings, distributions will be made according to the reorganisation plan approved by the court.

**Transactions that may be annulled****39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Under the BA, transfers involving assets of a reorganised company can be voided by court order.

Upon the written petition of the planner, a plan administrator or the official receiver, the court may order the cancellation and void the following transfers:

- a transfer of assets or transactions (or both) involving assets of the debtor carried out with the debtor's knowledge that it will prejudice creditors (except in the event the relevant beneficiary is not aware that such act or transaction would prejudice the debtor's creditors) (fraudulent transfer); or
- a transfer of the debtor's assets that intentionally provides preference to one or more of its creditors over other creditors, which is made in the three-month period prior to the commencement of proceedings under the BA or, in the event the creditors granted such preference are linked in some way to the debtor, within one year prior to the commencement of such proceedings (preferential transfer).

The BA provides that the following events, both in bankruptcy and reorganisation, invoke the presumption that the debtor and the beneficiary are aware that such a transfer or act would prejudice the debtor's creditors, and thus is a fraudulent transfer: the relevant transfer or act was made in the year before the filing of a bankruptcy petition or reorganisation petition, as the case may be; or the transfer was gratuitous or a transfer from which the debtor received an unreasonably small amount.

**Proceedings to annul transactions****40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

See question 36.

### Update and trends

An amendment to the BA (the Amendment) was published in the government Gazette on 24 May 2016 and applies to reorganisation cases filed after the Amendment came into force on 25 May 2016. The Amendment allows SMEs to enter into business rehabilitation, which is faster than the normal rehabilitation process. A new section has been added to the BA specifically for SME debtors to help an ordinary person or a juristic person who has debts of no more than 10 million baht to restructure debt more easily.

A debtor who may be placed under business rehabilitation according to this Amendment must meet the following conditions:

- conduct an SME business in accordance with the laws in relation to the promotion of SME businesses; and
- be registered with the Office of SME Promotions or another government agency in order to conduct such business.

A petition for business rehabilitation may be filed with the court in a case where the debtor:

- is insolvent; and
- owes at least one or more creditors the following amounts depending upon on the type of debtor:
  - at least 2 million baht if an individual;
  - at least 3 million baht if a limited partnership, registered partnership, non-registered partnership, group of persons or other juristic person specified in the Ministerial Regulation; or
  - at least 3 million but less than 10 million baht if a private limited company.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Under Thai law, the liability of the directors and officers is separate from the liability of the company.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

Currently, under Thai law, there are two types of company: private limited companies and public limited companies. The liability of shareholders in both legal entities is limited only to the amount, if any, unpaid on the shares that are subscribed by them. Under Thai jurisdiction, the doctrine of separate legal entity is strictly upheld. Hence, a parent or affiliated corporation can be held responsible for the liabilities of subsidiaries or affiliates only in the event that such parent or affiliated corporation has personally guaranteed the entity's debts or where it has made itself a co-debtor with its subsidiaries or affiliates.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

Under the BA, an 'insider' is defined as, inter alia, a director, a shareholder holding more than 5 per cent of the total number of the issued shares of the debtor's business, and their spouses and minor children. 'Non-arm's length creditors' are not defined in the BA.

Under Thai law, there is no specific restriction barring insiders or non-arm's length creditors from initiating insolvency claims.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

No, there is no process by which some or all of the assets of a business may be seized outside of court proceedings. However, secured creditors naturally have rights over the assets for which security is afforded to them by the debtor prior to the order of receivership of such debtor's asset, and need not file a claim for a repayment of debt provided that the secured creditor allows the official receiver to inspect such asset.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

The liquidation of the company is governed by the Civil and Commercial Code (CCC) and the BA. If the company wishes to enter the liquidation in a normal situation, the company must call a shareholders' meeting and appoint a liquidator to settle the affairs of the company, to pay its debt and distribute its assets. In addition, under section 1266 of the

CCC and section 88 of the BA, if the liquidator of the company finds that after the whole of the contributions or shares has been paid up the assets are insufficient to meet the liabilities, the liquidator must apply at once to the court to have the company declared bankrupt.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

Bankruptcy proceedings are concluded according to section 133 of the BA. Once the official receiver has made the final distribution of the assets of the debtor, or has ceased to take action under a composition, or when the debtor has no distributable asset, the receiver makes a report of the business and accounts for receipts and expenditures in the action for submission to the court and requests a court order for closure of the action.

Reorganisation proceedings are concluded according to section 90/70 of the BA if the debtor's executive, plan administrator, interim plan administrator, or the official receiver, as the case may be, finds the reorganisation of the business has been successfully completed pursuant to the plan. He or she must promptly report this to the court and request the court to order the termination of the reorganisation. If the court views that the company has successfully implemented the plan, the court will render the order to terminate the reorganisation.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

With respect to insolvency proceedings, Thailand follows the territoriality principle (as opposed to the universality principle). Foreign judgments or orders with respect to insolvency proceedings in other countries are not recognised under Thai law. Under section 178 of the BA, foreign creditors who are domiciled outside the kingdom can claim for repayment of debts in a bankruptcy action upon compliance with certain conditions. Thailand is not a signatory to any treaties on international insolvency or on the recognition of foreign judgments. Thailand has not adopted the UNCITRAL Model Law on Cross-Border Insolvency.

### COMI

#### 48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

Thai courts do not recognise the COMI but rather regard each debtor company as a separate entity from its group of companies. To determine

jurisdiction, Thai courts consider whether the debtor is domiciled in Thailand, or operates business therein, whether by himself or by representative, at the time an application is made to adjudge such debtor bankrupt, or within a period of one year prior to that, as prescribed by section 7 of the BA. If this appears to be the case, the debtor can be adjudged bankrupt by Thai courts who will only have jurisdiction over assets of the debtor that are situated within Thailand, pursuant to section 177 of the BA.

#### **Cross-border cooperation**

**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

Under Thai law, there is no legislation providing cross-border cooperation. Therefore, according to section 177 of the BA, a foreign bankruptcy or order for control of a debtor's estate has no effect on the debtor's assets in Thailand. In addition, Thai law does not provide for the recognition of foreign judgments. However, a foreign judgment may form part of the evidence in a case brought in Thailand on the same subject matter, and be considered as 'best evidence', provided the judgment is:

- final and conclusive;
- not contrary to Thai public policy; and
- given by a court of competent jurisdiction.

Thailand is not a signatory to any international treaties on insolvency or the recognition of foreign judgments.

#### **Cross-border insolvency protocols and joint court hearings**

**50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

While Thailand is not a party to any international treaty on insolvency or recognition of foreign judgments, it is generally accepted that a foreign judgment may form part of the evidence in a case brought in Thailand on the same subject matter, and shall be considered as the 'best evidence' for consideration of the court. It should be noted that foreign judgments should be final and conclusive, not contrary to Thai public policy, and given by a court of competent jurisdiction.

The Legal Execution Department under the Ministry of Justice has, however, recently amended the BA by adding new provisions that are in line with the UNCITRAL'S Model Law on cross-border insolvency, including access for foreign creditors and foreign representatives, recognition of foreign proceedings and relief, cooperation and communication, and concurrent proceedings. This new legislation will enhance the enforcement of debtor's assets in cross-border matters.

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The bankruptcies and reorganisations are generally governed by the Enforcement and Bankruptcy Law (EBL) numbered 2004. The EBL is mainly supported by the provisions of the following laws and regulations:

- the Turkish Civil Code (TCivC);
- the Turkish Code of Obligations (TCO);
- the Turkish Commercial Code (TCC);
- the Banking Law (BanL);
- the Law of Banks (LOB);
- the Law on Procedure of Collection of Public Receivables (LPCOPR); and
- the International Private and Civil Procedure Law (IPCPL).

Any failure by a debtor in paying his or her due debt despite the bankruptcy case is a general reason.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The court ruling the bankruptcy case and rendering bankruptcy adjudication is the commercial court. In addition to that, the commercial courts take decision for the approval of the composition proposed by the debtor, postponement of the bankruptcy of the capital companies or cooperatives and restructuring of them through reconciliation.

The enforcement court takes decision regarding examination of the complaints lodged against the transactions of the bankruptcy offices, supervision and inspection of the bankruptcy offices, election of the members to the bankruptcy administration, approval of the invoices of the administration, granting duration for the composition, appointment of commissar and giving extraordinary duration.

With the introduction of a three-tiered court system in Turkey, parties may appeal the decisions of the local courts before the regional appellate court. It is possible to refer the decisions of the regional appellate court's decisions to the 12th and 23rd Civil Chambers of the Court of Appeals.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

As a rule, only merchants are subject to bankruptcy. The following are considered to be merchants and subject to bankruptcy pursuant to article 18 of the TCC:

- collective companies;
- commandite companies;
- joint-stock companies;
- commandite companies with share capital;
- limited liability companies;
- cooperatives;

- foundations and associations operating a commercial enterprise in order to achieve their goal; and
- institutions and corporations established by the state, special provincial administration, municipality, village and other public legal entities for the purpose of being managed or commercially operated in accordance with the private law provisions pursuant to their own laws of establishment.

A special method of liquidation has been determined for banks, financial institutions and insurance companies.

Following opening of bankruptcy, any and all seizable goods, receivables and rights included in the property holding of the bankrupt will be delivered to the bankruptcy estate irrespective of where they are present. However, the assets that are not of seizable nature as specified in the laws related to the governmental properties and the assets included within the scope of article 82 of the EBL are not delivered to the bankruptcy estate.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

The state, special provincial administration, municipality, village and other public legal entities, the associations conducting activity for the public interest and the foundations spending more than half of their revenues for activities that are in the nature of public services are not considered to be merchants and, therefore, they are not subject to bankruptcy irrespective of whether they directly operate a commercial enterprise or they operate the same by way of a legal entity managed or operated pursuant to the public law provisions.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

The Savings Deposit Insurance Fund of Turkey (SDIF) gives financial support to the banks that may be subject to a bankruptcy proceeding because of a failure in paying their debts, as well as protecting them against the risk of bankruptcy. Many banks have been revitalised in the financial system and kept alive through a special sale transaction where the bank transferred to the SDIF selects the assets and liabilities wanted by the buyer and a separate closing balance sheet is issued for the transfer transaction.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

The most frequently applied method of ensuring a security is a mortgage imposed on the immovable properties. The mortgage will entitle the mortgagee to ensure the foreclosure of the pledged property that is registered in the land registry if the receivable is not paid when due.

Any receivable that is present or that has not yet arisen, but will probably arise may be secured with a mortgage (TCivC, article 881). Unless otherwise stipulated in the law (for example, articles 892 and 893 of the TCivC), an agreement regarding the mortgage should be

executed by and between the mortgagee and the mortgagor in the presence of a deed officer in order to impose a mortgage, and this mortgage should be registered with the land registry.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

Pledge may be created over all kinds of tangible and intangible negotiable moveables including the intellectual and industrial property rights and receivables. If any receivable secured under a pledge is not paid, the pledgee will collect his or her receivable by converting the moveable subject to pledge into cash money.

Lien is a right entitling the creditor to retain, as a security for his or her receivables, the moveables and valuable papers pertaining to the debtor which are in his or her possession and that should be returned until the debt is paid and to convert the same into cash money by giving a notice in advance.

Retention of title is created by way of a notarial deed followed by registration in the relevant special register (eg, vehicle registration record for a car) and, thus, limited to the certain kind of transactions.

Commercial enterprise pledge covers the trade name and company name of the commercial enterprise, the machinery, tools, instruments and motorised means of transportation (moveable operating equipment), the letters patent, brands, models and the intellectual and industrial property rights such as drawings and licences and is issued based on the Law of Commercial Enterprise Pledge (LOCEP) No. 1447 dated 21 July 1971.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

The creditors may initiate an enforcement proceeding or a lawsuit against the debtor. Assets of the debtor may be seized if the creditors win the relevant lawsuit or the enforcement proceeding so initiated is finalised. However, these actions or proceedings may take many years if an objection is raised by the debtor.

In addition to the foregoing, the creditors may cause a cautionary attachment to be imposed on assets of the debtor if certain conditions are satisfied. In this method, the creditors may temporarily seize the assets of the debtor based on a court decision in order to secure the timely payment of their pecuniary claim. The court taking decision for cautionary attachment may also decide for receipt of a security from the creditor. This security is received for the purpose of ensuring that the losses to be sustained by the debtor (and third persons) are met if the creditor requesting cautionary attachment loses the lawsuit in the future.

Foreign creditors are required to post a guarantee prior to the lawsuits and enforcement proceedings to be initiated in Turkey unless there is a bilateral agreement between their own country and Turkey in this direction or there is a regulation in this respect in a multilateral agreement to which their own country and Turkey are parties. With regard to this matter, the creditors that are citizens or companies of a state that is party to the Hague Convention of 1954 on Civil Procedure are exempted from making a down payment pursuant to article 17 of this agreement.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

A debtor who is subject to bankruptcy may submit a petition to the extent that he or she is unable to pay his or her debt to a competent commercial court requesting that a decision should be taken for its bankruptcy.

Furthermore, the persons authorised to represent a capital company or a cooperative (for example, the board of directors in the joint-stock companies) may request a decision for bankruptcy of the company or cooperative attaching the balance-sheet indicating that the liabilities of the company or cooperation are more than the assets thereof. The commercial court will decide for bankruptcy of the company if it believes that the liabilities of the company or cooperation are

more than the assets thereof and if the postponement of the bankruptcy of the company or cooperative is not requested.

### Bankruptcy liquidation

Concurrently with the bankruptcy decision, the bankruptcy liquidation is initiated leading to the following consequences that cannot be stopped even if the decision is appealed:

- any and all seizable assets, receivables and rights of the debtor will automatically constitute the bankruptcy estate;
- the right to initiate a claw-back action granted to the creditors for the cancellation of donations and fraudulent actions made by the debtor for the purpose of concealing the properties from the creditors prior to the seizure of the properties or a decision is taken for bankruptcy of the debtor will pass to the bankruptcy estate and such actions of nullity will be initiated by the bankruptcy estate;
- the debtor's power of performing any act over his or her properties will cease;
- as a rule, the proceedings initiated against the bankrupt prior to the initiation of the bankruptcy will be stopped upon initiation of the bankruptcy and they will be terminated following finalisation of the bankruptcy decision;
- any new proceeding cannot be initiated against the debtor during the bankruptcy liquidation;
- the civil lawsuits that are initiated prior to the bankruptcy and to which the bankrupt is a party as a plaintiff or defendant will cease to be in effect concurrently with the opening of the bankruptcy;
- the overdue receivables of the debtor except those that are secured under a mortgage or pledge will become due and payable concurrently with the opening of the bankruptcy;
- the non-pecuniary receivables will be converted into the pecuniary claims by the creditors thereof;
- interest will continue to accrue in the receivables included in the bankrupt's estate; and
- in certain cases, the creditor may exchange his or her receivable with the receivable from the debtor.

### Liquidation through composition with creditors (LTCWC)

Another method of voluntary liquidation is LTCWC where the debtor leaves his or her property holdings to the creditors and requests that these property holdings should be liquidated by the creditors. This method of liquidation is also in favour of the debtor since it protects the debtor against bankruptcy. Moreover, the debtor will get rid of his or her debts and discharged contrary to the debtor who is liquidated within the framework of the current bankruptcy procedure.

### Dissolution

Another method of voluntary liquidation is liquidation as described in the TCC. The company whose activity is terminated because of any reason other than bankruptcy will enter the process of liquidation within the scope of the TCC. In general, the liquidation is managed through the liquidator appointed from among the partners. If it is understood that the company is over-indebted, the liquidator should request the bankruptcy of the company under the same conditions.

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

If the receivable of a creditor wishing to initiate a proceeding against his or her debtor subject to bankruptcy through the way of bankruptcy is dependent on a bill of exchange (cheque, policy or bond), the creditor will refer to the procedure of (special) bankruptcy particular to bills of exchange or otherwise, he or she will refer to the procedure of general (ordinary) bankruptcy.

Ordinary bankruptcy will be commenced with the bankruptcy proceeding claim to be submitted by the creditor to the execution office. The bankruptcy proceeding will be terminated if the debtor pays his or her debt within seven days (or five days in a special bankruptcy) or otherwise, the creditor will initiate a bankruptcy lawsuit in the commercial court requesting that a decision should be taken for the bankruptcy of the debtor.

The commercial court may decide for depository injunction. Based on this depository injunction, the court will instruct the debtor to pay

his or her debt together with the interests and executive costs thereof or to deposit the equivalent of the debt and the accessories thereof in the court's pay office within seven days. If, following the depository injunction, the debtor fails to pay his or her debt (or does not deposit the equivalent of the whole debt) and the creditor deposits the necessary expenses in advance, the commercial court will decide for the bankruptcy of the debtor at the first hearing following the depository injunction.

The creditor may also directly initiate a bankruptcy lawsuit in the commercial court without sending a bankruptcy payment order to the debtor through submitting a bankruptcy proceeding claim to the execution office based on the following reasons:

- if the residential address of the debtor is not known;
- if the debtor escapes in order to get rid of his or her commitments;
- if the debtor commits fraudulent acts violating the rights of his or her creditors or attempts to commit such an act;
- if the debtor conceals his or her assets during a proceeding through attachment;
- if the debtor suspends the payment of his or her debts;
- non-approval of the composition proposed by the debtor or the removal or fully termination of the duration for composition;
- fully termination of the restructuring of a capital company or cooperative through mutual consent;
- any failure in paying a receivable based on a judgment although the same is requested through an execution order; and
- any occurrence where the assets of the capital companies and the cooperatives cannot meet the liabilities thereof.

If the Commercial Court determines the existence of the receivable and the above-mentioned reason of bankruptcy as a result of the investigation, it will directly decide for the bankruptcy of the debtor without rendering the depository injunction for the debtor.

Concurrently with the bankruptcy decision of the commercial court, the liquidation in bankruptcy regarding the debtor will have been commenced. Thereafter, the bankruptcy office will commence the liquidation process.

## Voluntary reorganisations

### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

#### Ordinary composition

A debtor may prevent his or her bankruptcy by declaring ordinary composition (off bankruptcy or bankruptcy preventive composition), which allows him or her to restructure debt by concluding a composition agreement irrespective of whether he or she is subject to bankruptcy or not. The debtor or each creditor authorised to submit bankruptcy petition will inform his or her composition project by attaching his or her balance-sheet and income statement in the enforcement court at the same locality as the headquarters of the debtor. If the enforcement court is convinced that the success of the project is probable and it is free of causing any loss on the part of the creditors, it will provide the debtor with a duration of a maximum of three months for composition and will appoint one to three commissars in composition.

No executive or bankruptcy proceeding can be made and the previously initiated proceedings will be stopped except the foreclosure of pledged property for the receivables obtained through the pledge of moveables and immoveables, and the proceedings through seizure for the employee's receivables against the debtor during the time period given for the composition. If the adjudication for the affirmation of the composition has not been concluded within the term, the court may, with due regard for the report of the commissioner with justification, decide to suspend the proceedings previously initiated against the debtor or not initiate new proceedings against the debtor to be valid for the period after the conclusion of the composition term.

During this period, the debtor may conduct his or her activity under the supervision of the commissar. Thereafter, the commissar will call the creditors and the creditors will decide whether to accept or reject the composition at this meeting.

For the acceptance of the composition, both the majority of the creditors (a majority exceeding half of the informed and written creditors should accept the same) and the receivable majority (the receivables of the informed and written creditors should exceed at least two-thirds

of the total receivable amount) should be ensured and the requirement of depositing a security should have been fulfilled. The privileged creditors and the pledgees are not included in this calculation.

If the creditors accept the proposed composition, this proposed composition will be affirmed by the commercial court. Thereupon, the debtor will pay his or her debts pursuant to the affirmed composition and get rid of that part of the debt waived based on the said composition.

#### Post-bankruptcy composition

The majority in the same ordinary composition is required for the acceptance of the post-bankruptcy composition. However, this time the proposal will be made to the bankruptcy administration and no duration is given and no commissar is appointed for the composition. The encashment will be postponed until the commercial court takes a decision for affirmation. The court will affirm the composition if it determines the existence of the necessary requirements and inform the same of the administration of bankruptcy when the decision is finalised. If the request for affirmation is rejected, the administration of bankruptcy will continue the transactions for the liquidation in bankruptcy following receipt of a notice in this respect.

#### Postponement of bankruptcy (POB)

The postponement of bankruptcy is the most frequently used reorganisation institution, and at the same time it is the most-criticised institution because it is extremely in favour of debtors. POB is an institution ensuring the improvement of the financial position of an over-indebted capital company or cooperative within the framework of the improvement project to be submitted by the company to the court and that involves taking the company under the court's protection and ensuring the improvement of the financial position of the said company.

The debtor or any creditor may request the postponement of the debtor's bankruptcy by providing the court with an improvement project indicating the objective and real sources including investment of new cash capital. The information and documents (eg, list indicating the payment terms and amounts of existing debts, addresses of creditors, inventories according to the features of the industry as well as their waiting period and amount, the latest balance sheet and income statement submitted to the tax office, trade registry certificate of the company or cooperative) proving that the improvement project is serious and persuasive should also be submitted to the court. In this respect, the debtor requesting the POB should have been over-indebted, the improvement project should be serious and persuasive, there should be the hope of improvement and the debtor should not have made use of the extraordinary duration.

Following receipt of the request for the POB, the court will promptly appoint a trustee for the preparation of an inventory (itemisation of the debtor's properties) and taking the place of the board of directors or for approval of the resolutions passed by the board of directors and it will take the other measures required for the protection of the property holding of the company and the cooperative.

A decision will be taken for the POB of the company if the improvement project of which has been found to be serious and persuasive.

The duration for the postponement of bankruptcy can be maximum of one year. This duration may be extended for a year more where it is found appropriate by the court taking into consideration the reports given by the trustee. A capital company or cooperative that has benefited from postponement of bankruptcy cannot make any demand for POB before a year passes following the expiration of the postponement period including any extensions, as the case may be.

The trustee will regularly submit reports to the court regarding the activities of the company, the bankruptcy of which is postponed at such time period to be determined by the court.

Following the decision for postponement, no proceeding including the proceedings conducted pursuant to the LPCOPR (including the proceedings related to the public receivables) can be conducted against the debtor and the previously initiated proceedings will be automatically stopped.

During the postponement, a proceeding may be initiated through the foreclosure of pledged property because of the receivables obtained based on an immovable or commercial enterprise pledge or it will be possible to proceed with the previously initiated proceedings; however, any protective measures cannot be taken and the sale of a pledged property cannot be realised because of such a proceeding. In this case, the

interest will accrue during the term of postponement and a security should be provided for the interests that cannot be met with the current pledge.

However, a proceeding through seizure may be conducted for the employee's receivables as provided for in the first sentence of article 206 of the EBL.

The bodies of the debtor will maintain their duties and authorities under the supervision of the trustee within the framework to be determined by the court. The rights and obligations of the debtor arising from the agreements executed prior to the decision of postponement will continue to be in effect. The fact that a decision is taken for the postponement of bankruptcy will not prevent the continuance of the previously initiated lawsuits or the initiation of new lawsuit during the term of postponement except the bankruptcy lawsuit.

Following the determination of the impossibility of an improvement at the end of the duration for postponement, the court will decide the bankruptcy of the debtor. Even if the duration of postponement has not expired, if the court comes to the conclusion, based on the reports delivered by the trustee, that the improvement of the company's or the cooperative's financial position is not possible, it may withdraw the decision for postponement and decide for the bankruptcy of the company or cooperative. If the improvement of the company is realised at the end of the duration for postponement, the decision of postponement will be removed and the company will continue to conduct its activities.

#### **Restructuring of capital companies and cooperatives through mutual consent (RSCCTMC)**

The institution for the RSCCTMC has been substantially arranged for the restructuring of the big undertakings' debts differently from the composition. However, the banks and insurance companies cannot file an application with this institution in the capacity of a debtor.

In order for the capital companies and cooperatives to benefit from this regulation, their applications should be prepared in good faith, they should be unable to pay their due debts or their current assets and receivables should not be sufficient to meet their debts or they should be on the verge such a situation.

If the capital company or cooperative in such a situation reaches an agreement with the majority of its creditors with whom negotiations are conducted, who are affected by the project and who have receivables at a certain rate, it may file an application with the commercial court of first instance in the same locality as the headquarters of the relevant capital company or cooperative for the restructuring of its debts.

It is sufficient for it to reach an agreement only with the creditors affected by the project. It is also possible for the debtor to create receivable classes among the creditors having similar receivables. In this case, each creditor category should accept the project based on a large majority as stipulated in the law. The necessary majority will be deemed to have been acquired if the restructuring project is accepted by the majority of creditors exceeding half of the creditors who are affected by the project and constituting at least two-thirds of the creditors participating in the voting. If the project contains more than one creditor class, each creditor class should have accepted the project based on the necessary majority within its own class. In addition to the foregoing, the debtor that has filed the application should indicate that the amount to be acquired as a result of the project by each creditor that has rejected the project will be equal to the amount to be acquired as a result of the liquidation in bankruptcy.

The restructuring project to be submitted to the commercial code will contain the following issues:

- the conditions governing the creditors affected by the project and the manner in which equality will be ensured among and between the creditors having similar receivables;
- the effect of the project on the agreements to which the debtor is a party;
- the effect of the project on the debtor's power to perform acts of disposal over his or her property holding;
- if it is deemed to be necessary for the restructuring of the debts, the issue of whether the debtor will apply for sources of financing such as loans;
- the methods that may ensure the applicability of the project such as the transfer of the debtor's undertaking in whole or in part, a merger with another company or companies, any change in the

capital structure or an amendment to the debtor's articles of association, determination of the persons who are going to take part in the management of the debtor's undertaking, extension of the maturity date of the debts, changing the interest rates and issue of moveables;

- the issue of how and by whom the implementation of the project will be controlled after the decision of approval; and
- the fact that the receivable of the creditor that has rejected the project will be subject to equal treatment with the receivables of similar nature with regard to quality unless the relevant creditor explicitly accepts an amount that is less than those stipulated for his or her own class in the project.

The court that has received the application will promptly take the measures it may deem necessary with regard to the activities of the debtor until the date on which the final decision regarding the application is going to be taken. Furthermore, the debtor may refer to the new financing instruments during this interim period.

The approved restructuring project and the conditions thereof prevail over the provisions of any and all agreements executed with the creditors affected by the project.

#### **Time extension in extraordinary cases**

In extraordinary cases and especially during periods of economic crisis, the government may decide that provisions regarding time extensions in emergency cases apply to affected debtors for a specific time period. If the debtor failing to fulfil his or her commitments in places determined by the government without any fault on his or her part hopes to pay all of his or her debts at the end of the time period, the enforcement court may grant an extension not exceeding six months to the relevant debtor.

Although a proceeding may be conducted against the debtor during the time extension given in extraordinary cases, these proceedings will not result in conservation, encashment or bankruptcy as long as the extension continues to be in effect.

#### **Involuntary reorganisations**

##### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

Although this is not observed frequently, creditors may also request postponement of bankruptcy and composition regarding the debtor under the conditions specified in question 11. However, creditors are not obliged to submit the commercial books, balance-sheets and income statements of the debtor, as well as not being obliged to deliver a composition project.

#### **Mandatory commencement of insolvency proceedings**

##### **13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

If any creditor or creditors of the debtor initiates a proceeding through attachment against the debtor and if this proceeding results in the disposition of half of the assets pertaining to the debtor and if the remaining assets of the debtor are not sufficient to meet the other debts of the debtor that may become due within one year, then the debtor will promptly inform them that he or she has become insolvent and request that the commercial court take a decision on his or her bankruptcy. If he or she fails to request his or her bankruptcy and goes bankrupt within one year, then the relevant debtor will be considered to be a negligent bankrupt and he or she will be penalised.

In cases where the assets of the company do not meet its liabilities in the capital companies and cooperatives, the board of directors in the joint-stock companies and cooperatives and the manager of the limited liability companies is obliged to request a decision for the bankruptcy of the company pursuant to article 376 of the TCC.

In cases where the debtors actually cause insolvency as a result of gross negligence in their business affairs or knowingly aggravate the situation, they may be subject to penal sanctions.

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### Doing business in reorganisations

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#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

The debtor may proceed with his or her business affairs under the supervision of the commissar in case of ordinary composition and under the supervision of the project controller in case of the RSCCTMC. However, the enforcement court may allow effective execution of certain transactions in the presence of the commissar or allow the commissar instead of the debtor to conduct the activity of the undertaking.

The debtor cannot impose any pledge, stand surety for someone, transfer or impose restrictions on any immovable or permanent installation of the undertaking and perform any voluntary act of disposal without obtaining permission of the enforcement court or otherwise, the transactions to be carried out will be null and void.

In case of the postponement of bankruptcy, the court may appoint a trustee who will take the place of the management or approve the resolutions to be passed by the board of directors. The debtor will continue to conduct his or her activity under the supervision of the trustee within the framework to be determined by the court. The court may take measures in the direction of extending or narrowing the restrictive decisions regarding authorised signatories of the company taking into consideration the operating reports to be given by the trustee regarding the undertaking.

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### Stays of proceedings and moratoria

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#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

As a rule, the proceedings initiated against the bankrupt prior to the initiation of the bankruptcy will be stopped upon initiation of the bankruptcy and they will be terminated following finalisation of the bankruptcy decision. Any new proceeding cannot be initiated against the debtor during the bankruptcy liquidation.

The civil lawsuits that are initiated prior to the bankruptcy and to which the bankrupt is a party as a plaintiff or defendant will cease to be in effect concurrently with the opening of the bankruptcy.

No executive or bankruptcy proceeding can be made and the previously initiated proceedings will be stopped except the proceedings except the foreclosure of pledged property for the receivables obtained through the pledge of moveables and immovable and the proceedings through seizure for the employee's receivables against the debtor during the time period given for the composition.

Following the decision for postponement, no proceeding including the proceedings conducted pursuant to the LPCOPR (including the proceedings related to the public receivables) can be conducted against the debtor and the previously initiated proceedings will be automatically stopped; the lapse of time and foreclosure durations that may be interrupted because of proceeding transaction will not be functional.

Commencement a foreclosure proceeding for the pledged properties and receivables of employees in accordance with article 206 of the EBL are exempted from the automatic stay.

In a manner covering the proceedings and lawsuits initiated pursuant to the LPCOPR, the court may take decision for the stay of the proceedings initiated by the creditors affected from the project and the lawsuits related to these proceedings, prohibition of the initiation of new proceedings for the affected creditors and for non-application of the decisions for preliminary injunction or cautionary attachment.

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### Post-filing credit

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#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Within the scope of ordinary composition, the debts incurred based on the approval of the commissar during the time extension in

extraordinary cases will be considered to be the debt of the bankruptcy estate in the composition through the abandonment of the property holding or in any future bankruptcy.

Within the scope of the RSCCTMC, the debtor may refer to the financing instruments like loan if the same is compulsory for the continuity of the undertaking or it is deemed to be necessary for the protection of, or for the purpose of increasing, the value of the property holding (the purchase of the necessary goods and service is also included within this scope). If it is necessary to give a security in order to use a source of financing, this security will firstly be insured over the debtor's moveables and immoveables on which any pledge has not previously been imposed.

The obtaining of a new loan by the debtor within the scope of bankruptcy liquidation is not possible.

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### Set-off and netting

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#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

During the process of liquidation, the creditor may set off his or her receivable with the bankrupt's receivable. However, no set off can be made in the following cases:

- if the debtor of the bankrupt becomes the creditor of the bankrupt following opening of the bankruptcy;
- if the creditor of the bankrupt becomes the debtor of the bankrupt or the bankruptcy estate following opening of the bankruptcy; and
- if the receivable of the creditor is dependent on a share certificate of bearer type.

Upon bankruptcy of the joint and limited liability companies and cooperatives, those parts of the share certificates that have not yet been paid or those that are subscribed to but not yet paid cannot be set off against the debts of such companies.

If the creditor creates a receivable against the bankrupt in order to obtain an interest for him or herself or a third person knowing that the debtor is in the status of insolvent prior to the opening of bankruptcy, such an exchange will be invalid.

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### Sale of assets

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#### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

Goods that may fall in value or the protection of which may be expensive will be sold without delay. The securities and goods that have a price at the stock exchange or at the market may be promptly converted into actual money. The other assets will only be sold after the second meeting of creditors. The other assets pertaining to the bankruptcy estate will be sold through public auction by way of the bankruptcy administration or through bargaining if so decided by the creditors. The assets bearing the right of mortgage thereon may be sold through bargaining only after having obtained the consent of the pledgee creditors.

In any case, flexibility has been accepted in the LTCWC and the procedure and time of encashment will be decided by the board of creditors. The property holding will be realised separately or as a whole and in case of any creditor, through the collection of this receivable or the sale of the right to claim, through bargaining or public auction for the other assets.

While the assets sold during the process of liquidation are sold without restriction and the assets sold outside the process of liquidation are sold together with the restrictions thereon.

There is no procedure regarding 'stalking horse' bids and in the sales during the liquidation, the creditors other than the mortgagees cannot deduct their own receivable from the tender price.

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**Intellectual property assets in insolvencies**


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- 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

The issue of whether the bankruptcy of either party may terminate the agreement will be firstly determined according to the legal regulations or according to the agreement in cases where there is no legal regulation or according to the legal nature of the agreement in cases where there is no provision in the agreement.

In accordance with articles 58/I and 59/II of the Law on Intellectual and Artistic Works, in case of the death or bankruptcy of the licensee of any financial right, the licence agreement will expire in cases where the exercising of the licence right is dependent on the personality of the licensee only. As a matter of fact, any personal ability or skill is not required while exercising the rights of reproduction and distribution.

In article 50/II of the Law on Intellectual and Artistic Works, the case of bankruptcy by the licensee prior to the completion of the work has been expressed as the reason for terminating the licence agreement.

In Turkish law, there is no legal regulation with regard to how the brand licence agreement will be affected from the bankruptcy. If there is a gap regarding the termination of the brand licence agreement, the provisions included in the similar agreements may be applied by analogy. For example, if the provisions regarding the ordinary partnership are applied for the brand licence agreement, the brand licence agreement will expire in cases as stipulated in article 535 of the Code of Obligations and in the existence of valid grounds to the extent the same complies with the duration, notice and concrete event and in the application of the provisions related to the ordinary partnership, the death, loss of ability, disappearance and bankruptcy will terminate the agreement.

The status of the patent licence agreement is explained making an analogy with the lease agreement. If the licensee goes bankrupt after the patent constituting the subject matter of the licence is delivered to him or her, article 332 of the TCO regarding the lease agreement will apply by analogy. In this case, the licensor may request security for the values of licence that are accumulated or that will arise from the licensee and the administration of bankruptcy. The licensor may terminate the licence agreement if the said security is not given.

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**Personal data in insolvencies**


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- 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

Following the enactment of the Law on Protection of Personal Data (the Law) on 7 April 2016, a general prohibition started to be applied in Turkey on processing or storing personal data without the express consent of the owner. Under the Law, there is no specific regulation for insolvent companies. Thus, all restrictions applied for any other processor will also be applied to the insolvent companies. Therefore, it should be ensured that the consent of the owner has been collected in compliance with the Law.

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**Rejection and disclaimer of contracts in reorganisations**


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- 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

In accordance with article 309/r of the EBL, any contract terms that may affect the application of the restructuring project shall not be applied against the debtor. However, this provision is only being stipulated under RSCCTMC provisions. Thus, article 309/r cannot be applied for other reorganisation institutions. However, as an exceptional case, if the agreement between the parties and the acts to be performed pursuant to the requirements of this agreement conflict with the measures

included in the improvement project submitted to the court by the debtor, a decision should be taken by evaluating the effect of the contractual acts on the debtor company.

The party of the agreement that is breached by the debtor may register its claim arising from the breach of contract to the bankruptcy estate. Those creditors are unsecured creditors.

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**Arbitration processes in insolvency cases**


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- 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

There is almost no way of incorporating arbitration into the bankruptcy. That is to say, the bankruptcy case will be initiated at the commercial court of the locality where the headquarters of the debtor are located.

In disputes arising after the opening of bankruptcy, the Administration of Bankruptcy may come to an agreement directly regarding the receivables up to an amount of 2,000 Turkish lira and based on the authority to be granted by the total of the creditors in case of the receivables exceeding the foregoing amount. The administration of bankruptcy may settle the disputes by way of arbitration if the authority to refer to arbitration is granted.

However, in a final decision taken by the Supreme Court of Appeals, it has been decided that the rule of not applying the arbitration clause in the bankruptcy cases will be effectual with regard to the state sovereignty for rendering a bankruptcy decision and this rule is not related to the phase of determining the receivable and at this phase, the arbitration clause should be valid.

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**Successful reorganisations**


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- 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

See question 11.

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**Expedited reorganisations**


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- 24 Do procedures exist for expedited reorganisations?**

There is no defined procedure for expedited reorganisations.

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**Unsuccessful reorganisations**


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- 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

In POB, the court will evaluate the request for postponement and if it comes to the conclusion that improvement is not possible, it will remove the decision of postponement and decide on the bankruptcy of the company.

If the concordat is not approved or the time extension is removed, a decision will be taken for the prompt bankruptcy of the debtor upon receipt of the request to be made by one of the creditors within 10 days following the announcement regarding this decision.

The court that has rejected the approval of the concordat will decide for the cautionary attachment of all attachable assets of the debtor without seeking any security. This decision will be applied based on the request of a creditor that has deposited the relevant costs as advance.

The provisions regarding termination of the concordat will apply in the RSCCTMC.

If the debtor fails to fulfil his or her obligations arising from the project in whole or in part, the court will determine whether the debtor has fulfilled his or her obligations as a whole or in part, the project is implemented and the revision thereof is not in question or the financing creditor cannot obtain its receivable in whole or in part, it will promptly decide on the bankruptcy of the debtor.

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### Insolvency processes

- 26** During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

The bankruptcy adjudication is published in a newspaper having a circulation of more than 50,000 and distributed throughout Turkey, and in a newspaper and trade registry gazette in the locality of the headquarters of the debtor. The closing and removal of the bankruptcy will also be informed and announced following the same procedure.

If the fact that the liquidation will be realised ordinarily is approved, the first meeting of creditors and the second meeting of creditors will be made and the creditors will be invited in accordance with the above-mentioned procedure. Apart from that, an invitation may be made for a new meeting of creditors if the majority of the creditors requests the same and the administration of bankruptcy comes to the conclusion that it is necessary.

The creditors are authorised to make the necessary inspection in the bankruptcy file.

The right to follow up an allegation the conclusion of which by the bankruptcy estate is not deemed to be necessary by the creditors will be transferred to the creditor wishing to do the same. The creditor that has taken over the same may continue with the proceeding.

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### Enforcement of estate's rights

- 27** If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

Creditors may pursue the allegations where the bankruptcy estate does not deem necessary to conclude. After having deducted the costs from the result to be obtained as a result of the creditor may be satisfied and the remaining amount will be deposited to the bankruptcy estate.

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### Creditor representation

- 28** What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

Establishment of a committee among the creditors for the liquidation in bankruptcy is not defined in the EBL.

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### Insolvency of corporate groups

- 29** In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

There is no special process of arrangement of bankruptcy within the group of companies. Any and all attachable assets of the bankrupt existing as of the opening of bankruptcy irrespective of the place thereof will constitute the bankruptcy estate and the same will be allocated for the payment of the receivables. In this respect, the bankruptcy process of each company will continue separately. If, however, the bankruptcy transactions of those who have undertaken a debt jointly coincide at the same time, a creditor may request all of his or her receivable from the bankrupt's estate of each bankrupt.

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### Appeals

- 30** What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

With the introduction of a three-tiered court system in Turkey, parties may appeal the decisions of the local courts before the regional

appellate court. It is possible to refer the decisions of the regional appellate court to the 12th and 23rd Civil Chambers of the Court of Appeals.

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### Claims

- 31** How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

Creditors should register and submit their claims providing the originals or certified copies of their evidence (share certificates and commercial book records, etc) within one month prior to the notification.

The bankruptcy administration will examine the claims following expiration of the duration for the registration of the claims and the alleged progress payments. Creditors may appeal the decisions of the bankruptcy administration with respect to their rank or rejected amounts.

There is no separate limitation or arrangement regarding the liquidation in bankruptcy with regard to the assignment of the claims by the creditors. In this respect, if, for example, the privileged creditor transfers this claim to another person, the preferential right will also pass to the creditor that has taken over the same.

The creditor may also have any claim that is dependent on a condition or maturity. Upon realisation of the condition or as of the due date the creditor may be satisfied.

The claims, the subject matter of which is not money, will be converted into pecuniary consideration. However, the bankruptcy administration may apply payment in kind for such claims. In this case, the administration of bankruptcy will give security if so requested by the creditor.

Concurrently with the opening of the bankruptcy, an interest will continue to accrue on the receivables included in the bankrupt's estate pursuant to article 196 of the EBL.

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### Modifying creditors' rights

- 32** May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The rank of the creditors determined previously based on the law cannot be changed and no agreement can be made in this respect, provided that article 376/3 of the EBL is reserved. If an objection is raised to the order of precedence, the court will examine the request and inspect the decision regarding the rank of the creditor within the framework of article 206 of the EBL and take the necessary decision.

Pursuant to article 376/3 of the TCC, an agreement may be executed in writing with the creditors for accepting the placement of their claims after all of the other creditors of a company whose assets do not meet its liabilities, whereby the amount of the debts owed to these creditors meet the deficit and resolve the over-indebtedness of the company thereof.

However, within the procedure of objection to the order of precedence, the court may examine the position of the creditor objecting to its rank and make a decision accordingly.

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### Priority claims

- 33** Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

In the liquidation in bankruptcy, the major privileged claims respectively consist of the secured claims, bankruptcy estate claims, public claims arising from a property and privileged claims accepted based on special laws and the claims written in the first three ranks of article 206 of the EBL. All other claims are non-preferential claims.

The public claims, such as customs duty, building and land tax and the inheritance and transfer tax required to be received from the properties constituting the subject matter of the pledge, will be paid prior to the secured claims.

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### Employment-related liabilities in restructurings

#### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

The bankruptcy, concordat or postponement of bankruptcy by the employer is not a reason terminating the agreement in Turkish law.

In case of the employer's bankruptcy, the worker's right to terminate the agreement will arise if a guarantee is not given within an appropriate time period even if the worker requests the delivery of a security for his or her wage after the bankruptcy from the bankrupt's estate pursuant to article 436 of the TCO. If the guarantee is given by the debtor or bankruptcy administration within an appropriate time frame, the worker will be obliged to proceed with the employment contract towards the bankrupt's estate.

If the employer becomes unable to pay its debts, the wages of employees and the accessories thereof (bonus, prim, profit share, commission, payments in kind) and their other rights and interests convertible to money (overtime wage, annual paid leave, weekend wage, national holiday and general vacation wages, severance pay, payment in lieu of notice) are protected.

The receivables of employees including the severance and notice pays accrued based on the business relation during a period of one year prior to the opening of bankruptcy and the severance and notice pays that they deserve after the termination of the business relation because of the bankruptcy have been considered to be privileged receivables and stated that they are going to be included in the first rank. In addition to the foregoing, the debts of the employers to the facilities or associations that were established for provident funds and other benevolent associations for workers and that have acquired the status of legal entity will also be included as privileged receivables in the first rank.

### Pension claims

#### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

The retirement and social security system is conducted by separate institutions completely independent of the employers. The necessary premium contributions should be paid to the social security institution. The receivables of the institution are enumerated as privileged receivables among the receivables included in the third rank in article 206 of the EBL.

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### Environmental problems and liabilities

#### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

Pursuant to article 534 of the TCC, the liquidation in bankruptcy will be conducted by the administration of bankruptcy in accordance with the provisions of the EBL. The bodies of the company will protect their representative authority for the issues where the company is not represented by the administration of bankruptcy. In this respect, the responsibility of the administration of bankruptcy is limited to the issues for which it is appointed pursuant to the provisions of the EBL and the authority and responsibility regarding all other affairs of the company will lie with the company officials.

In this respect, the bankruptcy estate is responsible for any failure in taking the necessary measures within the scope of the protection of the assets by the bankruptcy administration or office.

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### Liabilities that survive insolvency proceedings

#### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Pursuant to article 251 of the EBL insolvency certificates will be issued to creditors for the amount that has not been satisfied during the liquidation. After the closure of the bankruptcy liquidation process creditors holding an insolvency certificate may commence a proceeding against the debtor who has acquired a new property.

Under the LTCWC procedure, liabilities of the debtor do not survive as explained above.

In any reorganisation procedure, all liabilities of the debtor will survive.

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### Distributions

#### 38 How and when are distributions made to creditors in liquidations and reorganisations?

When the value of the sold assets is collected and the order of precedence is finalised, the bankruptcy administration will prepare the share table of the monies and make the final calculation. The administration of bankruptcy will inform every creditor of the nature and amount of his or her share. The distribution will be started upon expiration of the duration of the preparation of the share table and the final calculation. If there is any complaint, the distribution may be postponed at a rate by which the decision to be taken following receipt of the complaint may affect the distribution.

Temporary distribution may also be made upon expiration of the period for raising objections to the order of precedence (15 days as of the publication of the order of precedence). In this case a share may also be allocated for the disputed receivables that have not yet been finalised.

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### Transactions that may be annulled

#### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

The transactions that may be cancelled may be classified in three categories, voluntary acts of disposal, acts of disposal performed in the case of insolvency and acts of disposal intentionally performed for the purpose of causing damage.

The voluntary acts of disposal performed and the donations granted by the debtor during the last two years prior to the opening of the bankruptcy, except the ordinary and usual gifts, are subject to cancellation.

The following transactions carried out by the debtor during one year prior to the opening of the bankruptcy are subject to cancellation:

- the pledges imposed by the debtor for the purpose of securing a current debt except the cases where the debtor has previously undertaken to give a security;
- the payments made through any means other than money or usual means of payment;
- the payments made for an overdue debt; and
- annotations given to the land registry for the purpose of strengthening the personal rights.

Any and all transactions carried out by the debtor whose property holding is not sufficient for his or her own debts for the purpose of causing damage to his or her creditors may be cancelled in cases where the debtor's financial position and intention to cause damage are known or expected to be known by the other party of the transaction; provided that a proceeding should be initiated against the debtor through attachment or bankruptcy within five years of the date on which the transaction is realised.

If any action of nullity initiated by the Administration of Bankruptcy or a creditor pursuant to article 245 of the EBL is won, the assets constituting the subject matter of the lawsuit are taken to the bankruptcy estate as if they were owned by the debtor, they are sold by the administration of bankruptcy and the sales value will be allocated for the payment of the bankruptcy receivables. If the sales revenues of the assets meet all receivables and any amount remains at the bankrupt's estate, this money will be given to the defendant third person.

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### Proceedings to annul transactions

#### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

In general, the voluntary acts of disposal performed by the debtor during the last two years prior to the opening of the bankruptcy and

### Update and trends

Since the economic crisis of 2001 that took place in Turkey, POB petitions have been the most used tool through the process of turnaround and restructuring of capital companies and cooperatives. This restructuring tool has long stood on top among turnaround professionals as this tool allows capital companies and cooperatives to reorganise during the stay of execution period, which can continue for up to five or six years. However, the creditors and the financial markets have been complaining for many years that the POB is being misused by malicious debtors. These complaints were mainly stating that some companies were creating fictitious debt to apply for bankruptcy postponement, while others have been moving their headquarters to other cities to benefit from more bankruptcy-friendly courts.

As a result of such complaints of creditors against the misused applications, a new amendment restricting and posing a challenge to bankruptcy postponement applications was published in the Official Gazette No. 29,796 dated 9 August 2016 and has entered into force. It is crucial to note that government officials and financial market professionals also state that the POB should be replaced with a more transparent restructuring procedure that is hard to abuse. The government officials stated that research has been conducted for a different model than the POB procedure. From our point of view, the POB procedure should be replaced with a more balanced restructuring tool where the creditors' active involvement is required and the appointment of a restructuring or turnaround officer is mandatory.

existence of the cases as specified in 279 of the EBL during the previous one year are evaluated as being subject to cancellation. Similarly, any and all transactions carried out by the debtor during the period of five years prior to the date of proceeding for the purpose of causing damage to his or her creditors are also subject to cancellation. The right to initiate an action of nullity if the debtor goes bankrupt lies with the bankruptcy administration. If the administration of bankruptcy does not wish to initiate an action of nullity, it may transfer this right to any creditor wishing to acquire the same. The action of nullity is not initiated only in case of bankruptcy, but it may also be initiated when the fact that the creditor cannot receive his or her receivables is proven with a temporary or final insolvency certificate.

### Directors and officers

#### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

Generally, the obligations of the legal entities should be met from their own assets. The personal responsibilities of the managers arise if their obligations are violated. This responsibility will also be valid with regard to the public receivables.

### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

The conglomerate of companies has been regulated by the provisions of article 195 and the following articles of the TCC and the holding company cannot exercise its dominance in any manner causing damage to a subsidiary pursuant to article 202 of the TCC.

The loss experienced as a result of the directions of the parent company should be actually balanced during the same operating year or the affiliated company should be provided with the possibility of eliminating the said failure until the end of the current year at the latest.

Otherwise, each shareholder of the affiliated company may request that the loss sustained by the company should be indemnified by the parent company and its board of directors that has caused the said loss.

### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

A limitation with regard to the disputed receivables causing damage to the company or consequently to the bankruptcy estate and not complying with the accounts of the company may be in question. In this respect, the general provisions in questions 38 and 39 will apply.

### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

Except the process of bankruptcy and the liquidation in the meaning as specified in the TCC, the application of liquidation is possible within the scope of the processes of the transfer of the shares, assets or debts

of the company and the merger and demerger processes. However, the granting of a security or the payment of the debt may be in question for the protection of the creditors within the scope of these processes.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

Commercial partnerships are liquidated in two ways: according to the provisions of the EBL and the provisions of the TCC. In the case where the company goes bankrupt, the liquidation of the company will be realised in accordance with the provisions of the EBL. In the other cases of termination, the provisions of the TCC will apply. The liquidation procedures will be realised through two procedures: through the way of liquidation or without liquidation. The case of merger of the companies is a termination without liquidation.

Contrary to the liquidation through bankruptcy, the liquidation according to the TCC is not subject to the approval of a court.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

If the debtor submits a statement to the extent that all of his or her creditors have withdrawn their claims or a document indicating that all receivables are paid off or the executed concordat is approved, the court will decide for the removal of the bankruptcy and for the return of his or her assets in order to ensure the free disposal of them by the debtor.

After the monies are distributed, the administration will give a final report to the court that has taken a decision for the bankruptcy. Following receipt of this report and after having understood that the liquidation is completed, the court will decide on the closing of the bankruptcy.

### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

In order to ensure that the adjudications of bankruptcy or relevant decisions rendered by foreign courts or the other decisions taken within the framework of the bankruptcy procedure in the foreign courts have a result in Turkey, not only an enforcement proceeding, but also an action for recognition and enforcement should be initiated because of the nature thereof.

However, the Turkish courts may take a decision to the extent that the adjudications of bankruptcy rendered by foreign courts cannot be recognised because of the principle regarding territoriality of bankruptcy and the executive jurisdiction of Turkey with regard to bankruptcy cases.

**COMI****48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

It is compulsory for bankruptcy cases to be initiated in the court of the locality where the headquarters of the debtor are located without fail pursuant to article 154 of the EBL. As also specified in Supreme Court practice, the city centre where the headquarters of the debtors are registered with the trade register constitutes a presumption with regard to the headquarters within the scope of article 154 of the EBL. There is no special regulation with regard to the group companies. A special concrete evaluation is made for every company.

**Cross-border cooperation****49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

In the Turkish Bankruptcy Law, there is no special regulation for the cooperation between local and foreign courts and the administrations

of bankruptcy and for the recognition of foreign bankruptcy processes. In this respect, there are contradictions and differences both in the Supreme Court decisions and the doctrinal opinions with regard to the recognition of foreign bankruptcy processes. However, in order to enable the representative of a foreign bankruptcy estate to carry out any transaction in Turkey, the foreign award regarding the establishment and appointment of a bankruptcy estate and its representative should be recognised. In this respect, it will be appropriate to come to a conclusion after having examined the reciprocity principle and the other conditions regarding recognition according to the provisions of the international agreement and the IPCPL in every concrete situation.

**Cross-border insolvency protocols and joint court hearings****50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

There is no procedure regarding this matter.

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# United Arab Emirates

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

The insolvency regime in the United Arab Emirates (UAE) provides for liquidations, bankruptcies and reorganisations.

Liquidations of companies are governed by Federal Law No. 2 of 2015 (the Companies Law), with bankruptcy and reorganisation of traders being set out in Federal Law No. 18 of 1993 (the Commercial Code). Certain aspects of Federal Law No. 5 of 1985 (the Civil Code) and Federal Law No. 11 of 1992 (the Civil Procedures Code) also apply. Certain provisions of Federal Law No. 10 of 1980 concerning the Central Bank, the Monetary System and the Organisation of Banking apply on the bankruptcy or liquidation of banks and financial institutions.

The legislation is largely untested as there has yet to be a major corporate insolvency in the UAE. It is understood that in the past restructurings of companies have taken place on an informal basis, outside the processes provided for in the above laws. In some circumstances specific decrees have been issued to manage specific restructuring situations.

An example of one such special regime is the regime that applies to matters relating to the Dubai World group. Dubai Decree No. 57 of 2009 (the DW Decree) was issued by the ruler of Dubai to facilitate the restructuring of the Dubai World group. The DW Decree is a customised version of the Dubai International Financial Centre (DIFC) Insolvency Law and Insolvency Regulations. It disappplies many of the provisions of the DIFC Insolvency Law, with the apparent intention of ensuring that the restructuring of Dubai World will be carried out in a particular manner. Dubai World Group has a unique status as a decree corporation (established by decree by the ruler of Dubai) and as such was unable to restructure its debts under existing legislation. The DW Decree was therefore created to allow the specific debt restructuring of Dubai World Group, providing a formal framework that did not otherwise exist. The DW Decree does not have wider application and it is yet to be seen how or if the framework will be utilised elsewhere in future.

The limitations of the current federal legislation with respect to larger, more complicated corporate insolvencies have been recognised by the authorities and as such new draft insolvency legislation is currently in the process of being enacted (the draft form of this new legislation has already been approved by the UAE Federal Cabinet). One likely feature is reportedly a decriminalisation of 'bounced cheques' under certain circumstances.

The federal legislation mentioned above applies at a federal level. However, it should be noted that there are a number of free zones within the UAE, including the DIFC, a financial free zone created by the Emirate of Dubai. The DIFC can create its own legal and regulatory framework for all civil and commercial matters (UAE criminal laws continue to apply within the DIFC) and has done so. The DIFC Authority and the Dubai Financial Services Authority (DFSA) develop laws and regulations applicable to the operation of the DIFC and these laws are generally based on common, rather than civil, law. Laws have also been enacted in 2015 which set the basis for a new freezone in Abu Dhabi, the Abu Dhabi Global Market (ADGM). It is contemplated that once complete the ADGM's legal system will be similar to that of the DIFC.

Article 645 of the Commercial Code states that the criterion to determine if a debtor is insolvent is when the court (as referred to in

question 2) deems the debtor to have suspended payment of their commercial debts. This can be an actual suspension of payment at the time of maturity of the debts, because of the debtor's poor financial position and credit status. Alternatively, it may be imputed where a debtor uses 'abnormal' or 'illegal' methods to discharge its debts. Article 645 itself does not provide any further definition of an 'abnormal' method of discharging debt although the reference to other articles (specifically, articles 691, 878 and 890) suggests that resulting 'harm' and 'damage' may go some way towards indicating abnormality.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Although article 646 of the Commercial Code makes reference to a 'specialised court' to declare bankruptcy, in reality the UAE does not have a specialised bankruptcy court system. Bankruptcy processes are dealt with by the court where the trader or the relevant branch, agency or office of the trader is situated with the presiding judge of the relevant court referred to as the bankruptcy judge. Subject to criminal matters, which are heard by criminal courts, there are no restrictions on the matters that the court may deal with, provided the matters are bankruptcy-related. As noted previously, there is little, if any, experience of insolvency proceedings in the UAE.

Please note that pursuant to the DW Decree a special tribunal was established to decide disputes relating to the settlement of the financial position of Dubai World and its subsidiaries.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

In principle, the UAE courts have jurisdiction to hear bankruptcy cases relating to any commercial entity trading in the UAE that is a 'trader' conducting its principal activity in the UAE, or that has its central management in the UAE as defined in the Commercial Code. The definition of trader is very broad and, effectively, covers all commercial entities by virtue of either the form of entity or through the type of commercial activity undertaken. The bankruptcy provisions also apply to foreign 'traders' conducting their principal activity in the UAE or which have their central management in the UAE, even if no ruling declaring bankruptcy has been issued in a foreign country.

The Civil Procedures Code prevents seizure of 'public or private assets owned by the State or any of the Emirates' and this may be interpreted to prevent bankruptcy proceedings against state entities. In addition, state entities may be incorporated by decrees and these decrees may contain restrictions that prevent insolvency proceedings from being instituted.

Also exempted from the bankruptcy provisions set out above are certain individuals who have limited small businesses. While the definition of 'small business' remains unclear in this context, Chapter VII (Minor Bankruptcies) (article 800) may be applicable, where it is stated that if the insolvent's property valuation does not exceed 50,000 dirhams, the bankruptcy judge may (or as directed by

the creditors), have discretion to apply limited provisions 'in whole or in part' as specifically set out in the article itself.

UAE law authorises the courts to defer a declaration for bankruptcy for a period not exceeding one year provided that such company's financial strength is likely to be strengthened by such deferral or if it would be in the interests of the national economy.

As noted in question 1, specific legislation has been enacted in Dubai to facilitate the restructuring of the Dubai World group.

### Public enterprises

#### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

There are no special rules for the insolvency of government-owned enterprises. Note, however, the experience in relation to the Dubai World restructuring highlighted above.

### Protection for large financial institutions

#### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

The UAE has not enacted general legislation to deal with financial difficulties of institutions that are considered 'too big to fail', but some companies in financial difficulty have been considered for assistance on a specific case-by-case basis. For example, the Dubai government issued Decree No. 57 for 2009 in relation to the Dubai World restructuring. This decree adopted the insolvency laws of the DIFC as its basic legal framework but made a number of amendments to the DIFC insolvency laws that were only applicable to Dubai World. A similar decree – Decree No. 61 of 2009 – was also passed to establish a special judicial committee to consider and settle any petition or claim raised against Amlak Finance PJSC or Tamweel PJSC. Decree No. 61 effectively removes the jurisdiction of the Dubai Courts (the Court of First Instance, the Court of Appeal and the Court of Cassation), preventing them from hearing any claims in connection with Amlak Finance PJSC or Tamweel PJSC and further imposing the referral of all such cases to the special committee.

### Secured lending and credit (immovables)

#### 6 What principal types of security are taken on immovable (real) property?

Security over real property is usually taken in the form of a mortgage. Mortgages over real property may consist of:

- mortgages over freehold land and buildings constructed on such land;
- mortgages over leasehold interests in real property; and
- mortgages over buildings constructed on leased land.

The mortgage gives the mortgagee a security interest over the real property in question for the mortgagor's debt. As a result of the mortgage, the mortgagee obtains a priority right over unsecured creditors in general, although it is unclear whether certain preferred unsecured claims, including employee wage and tax claims, would be preferred over secured creditor claims. It should be noted that, other than in certain designated areas, restrictions on foreign ownership of real property exist throughout the UAE. In brief, each emirate is free to enact its own legislation in relation to foreign ownership of real property. In Dubai, the local population and nationals from Gulf Cooperation Council (GCC) countries can hold the title to freehold property without distinction though foreign owners may only hold the freehold title within specifically designated areas. There are also restrictions on the length of leaseholds.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

The principal types of security devices taken on moveable property are pledges, business mortgages, and assignments.

Pledges over moveables are effective if:

- possession of the pledged asset is transferred from the pledgor to the pledgee, or to a third party; and

- throughout the term of the pledge the pledged asset continues to be held in a manner that prevents the pledgor from disposing of the assets without the consent of the pledgee.

A business mortgage (a pledge over a commercial business) can be taken over a commercial business (usually interpreted to cover all the tangible and intangible property of a commercial trader); however, it may only be granted to banks and financial institutions. The items that are secured pursuant to a business mortgage should be in existence and identifiable and cannot be changed after perfection as the concept of a floating charge is not recognised. Business mortgages automatically expire after five years unless renewed. Because of the uncertainty of the UAE insolvency regime it is unclear whether a company's inventory or tradable assets would fall within the definition of a business mortgage. It should also be noted that while there may be some similarities between the business mortgage and an English law floating charge, the concept of a floating charge is not recognised under UAE law.

Pledges can be created over shares issued by some UAE incorporated companies although difficulties may arise for foreign creditors taking or enforcing such pledges because of laws restricting foreign ownership in UAE companies. In general, UAE companies must be 51 per cent owned by UAE or GCC nationals so the exercise of a pledge that results in non-UAE or non-GCC nationals owning more than 49 per cent of a company would be invalid.

Account pledges can also be created provided that the monies in the account are ascertainable and identifiable at the date of execution. There is a degree of uncertainty as to the consequence of a change in the initial balance as to the effectiveness of the security, but the conservative view is that every time the account balance fluctuates, the pledge needs to be taken again over the new balance.

Assignment agreements are usually taken as a form of security over contracts, contractual rights, account receivables and insurances. The Civil Code is silent as to whether it applies solely to the assignment of obligations or to the assignment of both rights and obligations. There is also uncertainty as to whether the consent of the obligor is required or an acknowledgment of the assignment in addition to a notice of the assignment. Under UAE law an assignment of future assets, which are not identifiable at the time the assignment is granted, is not permitted.

The perfection requirements for each type of security vary depending on the circumstances such as the location of the secured assets and the asset that is the subject of the relevant security interest. We note that separate perfection requirements are also applicable with respect to mortgages over certain property such as vessels and aircraft.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

In general, remedies are not available to creditors (secured or unsecured) outside of the formal bankruptcy proceedings. Pre-judgment attachments are not generally available, although creditors may have limited rights in situations where the creditor retains some right over a specific asset, for example where a creditor has actually retained physical possession of the 'thing' contracted for. The creditor is limited as to the actions it may take, it may not sell the asset in question unless it is of a type that would suffer loss or deterioration and the creditor must obtain court permission before proceeding to sell the asset. Retention does, however, provide the person retaining the goods a priority right over competing creditors.

We are not aware of any special procedures that apply to foreign creditors, other than extended deadlines for filing proofs of debt.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

The liquidation procedures set out in the Companies Law apply only to companies. The UAE distinguishes between:

- liquidations, which provide for the termination of the corporate existence of a company and the realisation and distribution of its assets of the company to satisfy any liabilities (where possible); and

- bankruptcies, which are principally aimed at discharging the debtor from its debts and liabilities and reorganisation in agreement with its creditors.

A company enters into 'liquidation' if it is dissolved. Joint liability, simple commandite (a company established by limited and unlimited partners) and joint-stock companies may be dissolved at the request of a shareholder where it appears to the court that there are serious grounds warranting the dissolution, or on the grounds of a shareholder's failure to meet its obligations. Events triggering dissolution include:

- expiry of the term set out in the constitutional documents;
- completion of the company's objectives;
- loss of all or most of the company's assets;
- merger; or
- a unanimous decision of the shareholders (subject to the terms of the company's constitutional documents).

Until the company is officially dissolved, the company retains its corporate existence to the extent necessary for the acts of liquidation. While the Companies Law sets out general guidelines in relation to the process of liquidation, a company is permitted to set out in its constitutional documents the manner in which it should be liquidated, or alternatively, the shareholders may agree on these details at the time of liquidation.

The liquidator, upon appointment, assesses the company's liabilities and assets. In addition, upon liquidation all debts owed by the company become immediately due and payable. The liquidator is required to notify all creditors and to invite them to present their claims in the liquidation within a time period of not less than 45 days.

If the liquidated estate does not have sufficient assets to discharge all outstanding debts, the debts are discharged between the creditors (and note the potential for bankruptcy proceedings to commence in that instance – see below). Any value that remains after all debts have been discharged is returned to the shareholders in proportion to each shareholder's equity in the company.

Once the liquidation has been completed and recorded on the Commercial Register the liquidation may be admissible as a defence against other parties, and the liquidator is required to request the deletion of the company from the Commercial Register.

Note that a company under liquidation may also be declared bankrupt by the court if the court is satisfied that the company is unable to pay its debts as they fall due. The creditors may petition for bankruptcy if a debt has become due and the debtor has ceased paying its debts or the debtor may make a petition for bankruptcy if approved by an EGM. The company may not be dissolved until bankruptcy proceedings have terminated and the proceedings are stayed from the time when a bankruptcy petition is presented to the court.

### **Involuntary liquidations**

#### **10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

There are two insolvency proceedings in Dubai: bankruptcy and liquidation, but as noted, liquidation proper provides for the voluntary termination of a company's corporate existence while the principal method for involuntarily winding-up a debtor is through bankruptcy proceedings.

Involuntary bankruptcy proceedings can be commenced by the public prosecutor, the courts or any creditor of a debtor. A creditor may apply for a declaration of bankruptcy in respect of any trader that fails to pay its debts when due. A trader who uses illegal or unusual means for paying its debts is regarded as being unable to pay its debts where these means suggest a poor financial situation.

The effects of an involuntary bankruptcy are similar to those of a voluntary bankruptcy. The court may make any order necessary to protect or administer the property of the debtor until a decision is made in respect of the bankruptcy. The court is required to send a copy of the bankruptcy declaration ruling to the Public Prosecution Service, the trustee, the Ministry for Economy and Commerce, the Chambers of Commerce, the Commercial Registry and the Central Bank.

Secured creditors are limited in the actions that they may take, as security cannot generally be enforced without a court order.

### **Voluntary reorganisations**

#### **11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?**

The Commercial Code recognises the concept of a composition to prevent bankruptcy and winding up (a protective composition). The protective composition is available to any trader other than a joint-stock company or a company in liquidation that has traded continuously for one year and has complied with all applicable laws. A trader may apply to the bankruptcy court for a protective composition notwithstanding an outstanding bankruptcy petition.

In addition to the one year's trading requirement, the applicant must:

- set out the cause of the 'disruption' to the business;
- provide a composition proposal; and
- file various papers and documentary evidence, including commercial accounts.

Upon filing a protective composition:

- a moratorium is placed on bankruptcy proceedings;
- the court may make protection orders to preserve the assets of the debtor (including restrictions on enforcement of security), until such time as a final determination is made on the protective composition application;
- the court appoints a trustee (who, in accordance with article 841(1) is appointed to 'initiate and follow up the proceedings of the arrangement') who registers the decision to open the composition procedures with the Commercial Register and publishes an invitation to creditors to attend a creditors' meeting in two daily newspapers;
- the debtor retains the right to manage his property under the supervision of the trustee;
- claims and executory procedures against the debtor are suspended; and
- the debtor cannot take loans, conclude a composition, pledge or transfer title without court permission.

Local creditors must submit details of debts within 10 days of publication of the notice, while foreign creditors have 30 days in which to submit the relevant details. Creditors who fail to submit documentation with respect to their debts lose the opportunity to participate in the composition proceedings; however, they may be bound by the terms of the composition.

Following receipt of the details of debts the trustee must:

- lodge details of the debts with the court;
- publish a final list of debts in a local newspaper; and
- send a statement to each creditor of the amount of the debt that he has accepted.

The debtor and creditors have 10 days within which to object to the published debts. Once the objection period has passed, the judge will prepare a final schedule of uncontested debts and must decide on any contested debts within 30 days of the final date for filing objections.

Once the judge has verified the debts, a creditors' meeting is held and the trustee submits a report on the financial situation of the debtor and his opinion on the proposed composition. Following the composition meeting, the judge must present the matter to court, which must ratify or cancel the composition. The court appoints one or more overseers from among the creditors to supervise enforcement of the composition.

It should be noted that a composition does not terminate debts or suspend interest on debts.

### **Involuntary reorganisations**

#### **12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?**

As noted above, a debtor may apply to court for a protective composition even after bankruptcy proceedings have commenced. If a debtor does not take advantage of the protective composition proceedings, the judge must commence judicial composition, which is an involuntary reorganisation proceeding.

Once judicial composition proceedings begin, the principal effect is that a creditors' committee is automatically formed and the creditors

whose debts have been accepted (either definitively or provisionally) are invited by the judge to attend a meeting to deliberate on a composition.

### **Mandatory commencement of insolvency proceedings**

#### **13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?**

A trader is required to file for declaration of bankruptcy within 30 days of the date on which it ceases to pay its debts. Any trader who fails to do so is deemed to have committed the criminal offence of bankruptcy by negligence.

A negligent bankrupt cannot be discharged until:

- the terms of any sentence imposed have been satisfied;
- all debts are repaid; or
- the composition is fulfilled (in the normal course of events a bankrupt is discharged three years from the date the bankruptcy is concluded).

Failure to file for bankruptcy within the 30-day deadline does not, however, prevent a debtor from instigating protective composition proceedings (as set out in question 11).

In the event of bankruptcy, under articles 878 and 879 of the Commercial Code, the debtor (or in the case of a company, the company managers), board members or liquidators, can be sentenced to imprisonment for a maximum of five years for bankruptcy by fraud. Under articles 880 and 881, bankruptcy caused by serious negligence carries a fine of 20,000 dirhams and a prison sentence of up to two years, whereas bankruptcy by negligence carries a fine of 10,000 dirhams and a prison sentence of up to one year.

### **Doing business in reorganisations**

#### **14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?**

The court may, at the request of the trustee or the debtor, give permission for the continuance of the business after bankruptcy proceedings are commenced. This decision is subject to appeal by the trustee or the debtor.

A debtor who files for protective composition retains the right to manage its property, although its management is under the supervision of the trustee (see question 18 for more information on the ability to sell assets). Any voluntary payments made by the debtor are not enforceable against creditors.

Creditors who supply goods or services after the filing are not subject to the terms of any judicial composition.

If a judicial composition is rejected, the trustee can only continue the business if:

- this is approved by 75 per cent of the creditors (both in terms of numbers and in terms of value); and
- the judge ratifies the creditors' authorisation.

Creditors can be held personally liable if the debts of the business increase after they have approved a continuation of the business.

### **Stays of proceedings and moratoria**

#### **15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?**

Upon pronouncement of a bankruptcy judgment, legal actions cannot be brought or pursued against the insolvent debtor except claims relating to:

- property or money that the debtor is not disqualified from managing;
- actions that the debtor may carry out during a bankruptcy;

- criminal actions; and
- matters that are reserved for final judgment.

The Commercial Code states that claims by ordinary creditors who hold general preferred rights are suspended at least until a date is specified for the sale of immoveable property. There is no method of self-help within the UAE and security interests cannot be enforced without a court order. However, creditors who have specific security may, subject to obtaining permission of the judge, make, or continue to make, claims against the trustee in relation to the specific property over which they hold security interests.

Dubai Decree No. 34 of 2009 has stayed all legal and judicial proceedings against the debtor in question.

### **Post-filing credit**

#### **16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?**

A debtor in a protective composition hearing cannot obtain credit or provide security without permission from the judge. Any transactions that are entered into in contravention of this stipulation are not enforceable against existing creditors.

While a trustee may continue the business of the debtor, it may do so only if it is in the best interests of the creditors or debtor. Management is generally supervised through monthly reports submitted to court. We are not aware of any priority that would be given to loans or credit given in these circumstances.

### **Set-off and netting**

#### **17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?**

The Commercial Code provides for set-off rights but certain requirements must be met before set-off or netting is enforceable on an insolvency. Set-off rights are enforceable in an insolvency to the extent that the obligations of the parties can be said to be 'connected'. A connection exists if the right and the obligation result from a single cause. Therefore, a UAE court may in fact regard two or more separate transactions as insufficiently connected, with the result that set-off or close-out netting provisions upon insolvency might not be recognised.

### **Sale of assets**

#### **18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

In a bankruptcy, the trustee's first obligation is to 'protect' the bankrupt's property and the trustee is generally restricted from disposing of assets without prior court approval.

Assets which are likely to deteriorate in value or which are costly to preserve may be sold upon order of the judge. A sale of assets may also be authorised if it is necessary to continue the bankruptcy or if it will result in a confirmed benefit to the creditors.

If a judicial composition is not accepted, the trustee is entitled to sell the property; however, a sale of 'all the assets at once' may only be done after seeking approval of the judge.

As assets can only be sold during a bankruptcy after an order from a judge, the court-ordered sale process should provide purchasers with a degree of certainty as to the title of the assets. A judge has considerable discretion when implementing the sale of any such assets (and in some instances, such as the sale of real estate, more specific rules can apply) but there is no legislative guidance as to what factors a judge would consider when assessing a credit bid whether from an assignee of the original secured creditor or otherwise.

In a liquidation, the liquidator must protect the company's assets and must sell assets by public auction, unless his letter of appointment

provides for the sale of assets to be conducted in some other manner. The liquidator is restricted from selling the entire business unless this is approved by the shareholders of the company. The company is bound by transactions concluded by the liquidator, provided these are required by the liquidation and are within the limits of his authority. These provisions should provide purchasers with some degree of certainty as to the title of the assets.

Given the requirement for judicial involvement in asset and business sales in bankruptcy and liquidations, there is limited scope for a system of 'stalking horse' bids. The UAE system does not specifically provide for credit bidding in sales, however one cannot discount using such a mechanism where to do so would be in the best interests of creditors.

### Intellectual property assets in insolvencies

**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

The Commercial Code does not specifically address this issue, although the general provisions of the Commercial Code on termination of contracts would apply (see question 21).

### Personal data in insolvencies

**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

The UAE does not have any specific data protection law comparable to those applicable in Europe outside of certain free zone areas such as the DIFC and ADGM. However, certain provisions in a number of different UAE laws may provide some protections in respect of privacy and the transfer of data.

For example, article 378 of Federal Law No. 3 of 1987 (the Penal Code) provides that the publication of any personal data that relate to an individual's private or family life is an offence. In addition, certain sector-based laws and policies, such as the Cybercrime Law and Privacy of Consumer Information Policy, require service providers to take measures to prevent the unauthorised use or disclosure of personal data.

Further, there are no specific provisions under UAE federal law that impose any obligations on data controllers to ensure data are processed properly. Notification or registration is not required before processing data provided that consent has been obtained from the data subject in relation to the collection and processing of any personal data relating to the individual's private or family life. There are no specific provisions under UAE law regulating the transfer of data. However, under article 378 of the Penal Code, data subjects should provide consent to the transfer of personal data to third parties inside or outside the UAE if that data relate to an individual's private or family life.

### Rejection and disclaimer of contracts in reorganisations

**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

A declaration of bankruptcy does not entail the dissolution of binding contracts; however, the Commercial Code allows the trustee to choose:

- not to implement contracts; or
- to discontinue contracts.

Where the trustee wishes to take either of the above actions it must first obtain the permission of the judge. If the contract is discontinued or not implemented, the counterparty is entitled to prove in the bankruptcy proceedings for compensation as an unsecured creditor.

The legislation does not provide further detail on the subject and the question of determining this has not to our knowledge been addressed as the legislation is largely untested.

### Arbitration processes in insolvency cases

**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

The Commercial Code provides that the trustee may accept arbitration in any proceedings connected with the bankruptcy, subject to obtaining consent of the judge where the arbitration relates to an indefinite amount or an amount above 10,000 dirhams. However, as with other legislation relating to insolvency, this is largely untested. Matters are able to be referred to arbitration by the judge after the case has opened provided that both parties consent to arbitration; however, as with other legislation relating to insolvency, this is largely untested in the UAE.

### Successful reorganisations

**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

A successful judicial composition must be approved by:

- a majority of creditors (50 per cent in number and holding at least two thirds of the outstanding debt);
- the judge overseeing the composition;
- the general assembly of the bondholders if the debtor is a company that has issued debentures exceeding 20 per cent of its total debt; and
- the court.

In respect of a protective composition, the plan must:

- provide for at least 50 per cent of outstanding debts to be paid within three years from the ratification of the terms of the composition;
- be accepted by a majority of the (voting) creditors whose debts are accepted or provisionally accepted and that amount to at least two-thirds of the outstanding debt;
- be accepted by the general assembly of the bondholders if a company has issued debentures exceeding 20 per cent of its total debt;
- provide for guarantees if the creditors so request; and
- be ratified by the court.

Secured creditors are not permitted to participate in a judicial or protective composition vote unless they waive their security interests.

The composition applies to all unsecured creditors (or creditors who have waived their rights to security) whether or not they have submitted to the composition.

UAE law does not provide guidance on the release of non-debtor parties from liability through a reorganisation plan (see question 41 for liability of officers and directors).

### Expedited reorganisations

**24 Do procedures exist for expedited reorganisations?**

The UAE does not provide for 'pre-packaged' reorganisations in any formal manner although it is possible that expedited reorganisations may have taken place informally outside of the legislative framework.

### Unsuccessful reorganisations

**25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?**

A judicial composition may be defeated by:

- failure to obtain approval;
- failure to obtain approval of the judge;
- the bankrupt is convicted of fraudulent bankruptcy; or
- failure by the bankrupt to comply with the terms of the composition.

If the composition fails, a creditors' committee is formed and it may replace the trustee. The trustee may only continue the business of the company if he receives the approval of 75 per cent of the creditors and the continuation is subject to the terms set out in the approval (notwithstanding any prior authorisation to continue the business). As noted in question 14, continuation is not without risk to the creditors. Following a failure of the composition, the trustee has the right to sell the bankrupt's property, to collect debts due and to make compositions with creditors.

A protective composition may be defeated:

- if it does not provide for payment of at least 50 per cent of outstanding debts within three years of the date of ratification of the protective composition;
- if the debtor has concealed property, fabricated or deliberately exaggerated debts; or
- any requirement for a successful composition is not achieved.

If the debtor fails to fulfil the terms of a composition, an application may be made for the dissolution of the debtor.

### Insolvency processes

#### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

Upon acceptance of a bankruptcy petition, the court sets a date for a hearing and notice must be given to all creditors informing them that they may notify the court of any debts on or before a specified date. If the court makes a bankruptcy judgment, the date of cessation of payments is recorded in the Commercial Register and the bankruptcy ruling is displayed publicly at the courts for a period of 30 days.

The bankruptcy judgment is also affixed at the place of business of the trader and the trustee is required to publish:

- a summary of the judgment in one or more daily newspapers within 15 days of the judgment; and
- an invitation to creditors to register their debts.

Creditors are also notified if their debts are disputed and of the final schedule of debts compiled by the bankruptcy trustee. If a creditors' committee is formed, an invitation to attend the composition meeting is published by the bankruptcy judge in a daily newspaper. If a consensual restructuring is not achieved, the bankruptcy judge invites creditors to attend a meeting to review the state of the bankruptcy. In general, notices can be provided to creditors by way of publication in daily newspapers; however, the manner in which creditors must be notified is not, in all cases, set out in detail in the relevant legislation.

The bankruptcy trustee's reporting obligations are principally to the court and the overseer. For example, the bankruptcy trustee must record all actions relating to the administration of the bankruptcy and these records may be inspected by the court and the overseer at any time. In addition, the bankruptcy trustee must submit a status report to the court every three months. The overseer may request information from the bankruptcy trustee on the progress, procedures and expenses incurred by the bankruptcy trustee.

If a creditors' committee is formed, the bankruptcy trustee must present a report on the status of the bankruptcy and related actions to the creditors' meeting.

As set out in other questions, a creditors' committee may be formed and this can approve or reject compositions. Any actions relating to bankruptcy require the approval of a judge, therefore actions against third parties (or the decision to release the liabilities of third parties) would have to be taken by the trustee or with the permission of the judge (other than in situations where assets are insufficient to cover the debts) (see question 27).

### Enforcement of estate's rights

#### 27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?

The bankruptcy laws do not provide for creditors to pursue the estate's remedies while the bankruptcy proceedings are continuing. However, if the bankruptcy is closed because of insufficiency of assets in the estate, creditors regain the right to commence individual proceedings against the bankrupt, but the relevant legislation does not discuss the possibility of creditors pursuing the estate's remedies. Given the limited experience in the country of insolvent liquidations we are not aware of any cases where a court has granted creditors the right to pursue the estate's remedies.

### Creditor representation

#### 28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?

The two principal committees that can be formed are those relating to protective compositions and judicial compositions. They are not 'committees' in the true sense of the word but are the body of creditors who have a right to vote on the protective or judicial composition, as the case may be. If a protective composition is approved by the creditors, an overseer is appointed to ensure that the conditions of the composition are implemented. The law suggests that the overseer should be a creditor but does not explicitly exclude the appointment of a professional adviser to this position; however, the relevant legislation provides that the overseer shall not receive a fee in relation to this work. While it may be open to the creditors to pay the overseer for acting in this capacity, the wording of the legislation suggests that such a fee would not be paid out of the debtor's estate.

### Insolvency of corporate groups

#### 29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?

The UAE insolvency regime does not provide for group insolvencies; however, the legislation is largely untested as there has yet to be a major corporate insolvency in the UAE. As noted in question 1, the DW Decree was passed specifically in respect of the restructuring of the Dubai World group and should the need arise to deal with a large group restructuring the issuing of a similar decree cannot be ruled out. Other large corporate reorganisations may have occurred outside the formal legal framework and it may be that group restructurings are also dealt with outside the formal insolvency framework.

The UAE is not party to any international insolvency or restructuring treaties and the Commercial Code, the Companies Law and the Civil Code are silent on whether assets could be transferred from a UAE administration to a foreign administration.

### Appeals

#### 30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?

Article 663 of the Commercial Code states that appeals related to bankruptcy proceedings should follow the procedures and periods stipulated under the Civil Procedures Code. In summary, the Civil Procedures Code stipulates that, in relation to the three levels of courts (court of first instance, court of appeal and court of cassation):

- appeals are dealt with in articles 150-188 of the Civil Procedures Code. The time for appealing against a judgment runs from the date following the date of the passing of the judgment (unless the law provides otherwise), and there is a time limit for making appeals of 30 days (or 10 days in expedited matters);

- permission to make an appeal is not required – it is an automatic right, but it is dependent on the sum in dispute (over 20,000 dirhams for court of appeal, and over 200,000 dirhams for court of cassation, except for where the sum claimed hasn't been evaluated); and
- appeals against a decision of the court of first instance can be made in relation to issues of fact or law whereas appeals against a decision of the court of appeal of cassation can only be made in relation to matters of law.

## Claims

### 31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?

All creditors, including secured creditors, must submit proof of debt to the trustee within 10 days of publication of the bankruptcy ruling. If creditors fail to do so, the trustee is required to publish a notice in a daily newspaper calling for local creditors to submit proof of debts within 10 days of the date of the notice (or within 30 days for creditors located abroad).

If the trustee or the debtor disputes a debt or security, the trustee must inform the relevant creditor immediately. Local creditors have 10 days in which to clarify a dispute (or within 30 days for creditors located abroad) and after such time the trustee must submit a statement of the debts to the court, along with any reasons for objecting to them and his opinion as to whether each debt should be accepted or rejected. Within five days of lodging this statement the trustee must publish the details in a newspaper and inform each creditor of the sum that he believes should be accepted in respect of the applicable debt. Both the creditors and the bankrupt have 10 days in which to object to final debt (or within 30 days for creditors located abroad). The judge has an independent right to contest a debt, even if no objection has been raised by the trustee or debtor.

If a debt is contested, the judge must rule on the contested debts within 30 days of the final date for objections. The judge's decision can be contested but this cannot delay the bankruptcy proceedings. Third parties can contest the bankruptcy ruling but must do so within 10 days of the ruling.

The law does not restrict creditors assigning their debts, nor does it set out any disclosure requirements.

Claims for contingent or unliquidated amounts can be submitted to the trustee. The court may, prior to making a final ruling with regard to a debt, provisionally accept a debt in an amount specified by the court. However, as noted above, the trustee, debtor and court may challenge a debt. The law does not provide any further guidance on how claims for contingent or unliquidated claims would be valued or on the nature of the proof required to be submitted by a creditor. The law does not provide further guidance on the enforcement of a claim acquired at a discount nor claims relating interest accrued after the opening of an insolvency case and the area relating to claims remains largely untested.

## Modifying creditors' rights

### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The relevant legislation does not specifically provide grounds for changing the rank of a creditor's claim, although it should be noted that while the Commercial Code gives priority status to employee salaries (which should be paid from the first cash to enter the bankrupt estate) the Commercial Code also states that public funds that are used to cover costs of the bankruptcy should be reclaimed out of the first cash that enters the bankrupt estate 'with priority over all creditors'. It is unclear from the Commercial Code how priority claims (including those of secured creditors) rank among themselves. Again, the legislation is largely untested and it is therefore unclear how the courts would approach this matter.

## Priority claims

### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

In addition to certain employee claims (see question 34), the Commercial Code provides for the following priority claims:

- certain preferred claims, including rent due on business premises and government taxes for the two-year period preceding the bankruptcy judgment; and
- bankruptcy costs and expenses.

Under the UAE insolvency regime, secured creditors are considered as 'preferred' creditors with rights over the assets pledged, although it remains unclear whether the courts would grant priority to the secured creditors or the priority claimants listed above.

## Employment-related liabilities in restructurings

### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

An employee who is terminated during a restructuring or liquidation is entitled to claim all rights provided for under the terms of the relevant employment contract. In the majority of cases, this would include unpaid wages and salaries, end of service benefits, accrued annual leave and repatriation costs. The Commercial Code gives priority status to wages and salaries due to the employees for the 30-day period prior to the insolvency.

The Commercial Code permits the bankruptcy trustee to terminate contracts, provided this is done in accordance with the provisions of Federal Law No. 8 of 1980 (the Labour Law).

The Labour Law provides for two principal types of employment contract, definite or limited-term and indefinite or unlimited-term contracts. The termination provisions differ between the two types of employment contracts and consequently the claims that may arise differ.

Where a limited-term contract is terminated for reasons other than fault on the part of the employee, the employee is entitled to an amount equal to three months' salary or payment of the remainder of the term of the contract, whichever period is shorter.

In the case of unlimited-term contracts, such contracts can be terminated for a valid reason (which would include restructuring or insolvency) at any time, by giving the employee at least 30 days' notice in writing. If such a notice is not given, and the employee is terminated, the employee is entitled to compensation in lieu of notice.

## Pension claims

### 35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?

The majority of employees in the UAE do not benefit from pension plans but are entitled to an end-of-service benefit, the amount of which depends on the employee's base salary and length of service. These end-of-service benefits do not constitute priority status claims under the Commercial Code; however, the Labour Law provides that all amounts due to employees have priority over the employer's property and must be settled immediately after judicial expenditure, amounts due to the public treasury and shariah alimony awarded to a wife and children. As noted in question 34, it remains unclear how priority claims would be ranked among themselves. Please note that separate rules may apply where the employees to be terminated are UAE nationals.

## Environmental problems and liabilities

### 36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?

The Companies Law provides that corporate officers and directors are liable towards the company shareholders and third parties for acts of

fraud, abuse of power, violation of the company's constitution and mismanagement of the company. Corporate officers may be liable to pay amounts owed by their corporations where the liabilities arise from any of the above acts. This provision applies regardless of whether the company is in an insolvency situation. The Commercial Code does not specifically address environmental issues and liabilities.

The UAE has specific environmental legislation both at a federal level and in each emirate. The main federal law is Federal Law No. 24 of 1999 Concerning the Protection and Development of the Environment; however, this is of general application and does not cover liability on insolvency.

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#### Liabilities that survive insolvency proceedings

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##### 37 Do any liabilities of a debtor survive an insolvency or a reorganisation?

Although the UAE insolvency regime is unclear on this matter, we understand that in the normal course of events, liabilities survive only if the reorganisation is unsuccessful. A protective composition may include a condition that debts must be repaid if the debtor becomes solvent within five years of the date of the composition.

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#### Distributions

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##### 38 How and when are distributions made to creditors in liquidations and reorganisations?

The legislation does not provide detailed guidance on how and when distributions will be made in a liquidation. Liquidations must be carried out in accordance with the terms of letter of appointment and this may include details as to timing of collecting in assets and distributing payments to creditors.

In respect of a reorganisation, if a composition has been finalised, distributions shall be made pursuant to the terms of the composition. The Commercial Code does not specify timing or the manner in which distributions must be made in other circumstances.

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#### Transactions that may be annulled

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##### 39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?

After the declaration of bankruptcy has been made the following transactions may be annulled or set aside and are not binding on the general body of creditors:

- gifts, with the exception of small presents that are customary;
- payment of debts before the repayment date;
- payment of debts with something other than that agreed; and
- providing security or guarantees for a pre-existing debt.

The Commercial Code also provides that any other transaction that is detrimental to the creditors can be set aside if the contracting party is deemed aware that the debtor was insolvent at the time of entering into the contract. The combined creditors may make a claim for restitution and the contracting party must return anything obtained from the debtor, profits resulting from the transaction and fees, if applicable. The contracting party is entitled to claim for restitution of any consideration provided.

The liquidation rules, the primary aim of which is to voluntarily dissolve a commercial entity, do not provide guidance on cancelling transactions. If a company under liquidation subsequently moves into the bankruptcy regime the above transactions may be annulled or set aside.

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#### Proceedings to annul transactions

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##### 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?

The UAE recognises a concept similar to a 'suspect period' in relation to the transactions referred to in question 39. The formal suspect period runs from the date on which the debtor is deemed unable to pay its debts. The Commercial Code permits the courts to provide for a date of

'cessation of payments' of up to a maximum of two years from the date of the ruling declaring the bankruptcy so the suspect period may run for a maximum of two years prior to the date of the bankruptcy ruling.

The Commercial Code provides that only the trustee may claim that detrimental transactions by the debtor should not be enforceable against creditors. The legislation relating to liquidation does not discuss suspect periods or cancellation of a transaction; however, as noted above, a company under liquidation may be declared bankrupt and transactions that it carries out may therefore be caught by these provisions.

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#### Directors and officers

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##### 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?

The Companies Law provides that corporate officers and directors are liable towards the company shareholders and third parties for acts of fraud, abuse of power, violation of the Companies Law or of the company's constitution and mismanagement of the company.

Corporate officers may be liable to pay amounts owed by their corporations where the liabilities arise from any of the above acts. This provision applies regardless of whether the company is in an insolvency situation.

In a corporate bankruptcy, the court may order the directors to pay the outstanding debts of the company. This possibility arises where the assets of the company are insufficient to pay at least 20 per cent of the company's debts. The orders may be made against the board of directors as a whole, or against individual directors and in an amount decided by the court.

The Commercial Code provides for imprisonment where directors have acted in a fraudulent manner (eg, by concealing or altering the company books and embezzlement) but the law does not specifically refer to any additional financial penalties.

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#### Groups of companies

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##### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

As a general principle under UAE law, each legal entity has a separate legal personality. Shareholders of companies such as LLCs and PJSCs are not liable for the debts of the insolvent company. Notwithstanding this, it is possible under UAE law to pierce the corporate veil in certain limited circumstances, but this area of law is not very well developed and there are few published cases. In particular, decisions of the UAE courts suggest that a shareholder can be directly liable to the company's creditors in situations involving fraud, deceit and negligence or serious error in its dealings with the company's creditors – although it is worth noting that these judgments have not been directly related to insolvency or restructuring cases. The relevant legislation does not provide any guidance on how and when distributions of group company assets (including assets owned by a group entity) will be made but – as highlighted previously – the judge has considerable discretion when considering such distributions.

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#### Insider claims

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##### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

There are no provisions under UAE law that specifically deal with limitations on claims by insiders and non-arm's length creditors in the manner this is dealt with in more sophisticated jurisdictions. We note that, under UAE law, however, courts have general discretion to invalidate and reverse transactions that are entered into on a non-arm's length basis or those that are entered into with third parties if such third party knew at the time it entered into the relevant transaction that the company had stopped repaying its debts.

**Creditors' enforcement****44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

We are not aware of any such processes that would permit creditors to seize assets outside of court proceedings.

**Corporate procedures****45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?**

As noted in question 9, the Companies Law sets out the procedures for liquidating a company while the Commercial Code regulates bankruptcies of traders. The aim of the two proceedings is somewhat different, as a liquidation involves the dissolution and termination of the corporate identity of a company, while bankruptcy aims to rehabilitate the debtor.

**Conclusion of case****46 How are liquidation and reorganisation cases formally concluded?**

A composition is formally concluded by ratification and publication of a notice by the court, with a summary published in the press. The composition must also be recorded in the relevant registration department where real property is located, establishing a charge over the property to secure the rights of creditors to whom the composition applies. The charge is released once the terms of the composition have been fulfilled.

In a liquidation the liquidator is required to pay all the debts owed by the company in liquidation. Once this has been completed, the liquidator must present a final account to the company's shareholders or the general assembly. Following presentation of the final account the liquidator registers the completion of the liquidation on the Commercial Register. Registration on the Commercial Register is deemed notification to the public. The final step in a liquidation is the formal removal of the company's registration from the Commercial Register that follows on from the registration of the liquidation.

In bankruptcy, the proceedings are terminated by the debtor's debts being fully discharged or the debtor providing the bankruptcy trustee with an amount sufficient to discharge its debts and expenses or upon the ratification by the court of the judicial or protective composition plan. Once the company has discharged its debts and the bankruptcy proceedings have been concluded, the company can continue trading and a court order granted for its rehabilitation.

Bankruptcy can, in practice, lead to liquidation proceedings. After the debts have been discharged, if the company's remaining assets are insufficient to carry on its business, the court may decide to make an order to dissolve the company, or the company may choose to voluntarily dissolve itself, as mentioned above.

**International cases****47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

The provisions relating to liquidation apply to foreign companies that conduct their principal activity in the UAE or have their centre of management in the UAE.

As noted elsewhere, there has yet to be a major corporate insolvency in the UAE and the general insolvency regime is largely untested. In addition, there is no specific legislation that deals with foreign insolvencies that may have a link to the UAE. As a result, it is likely that any such proceedings would be dealt with under normal UAE private international law and would therefore have to be enforced in accordance with the rules on enforcement of foreign judgments. Foreign judgments are not automatically enforceable in the UAE and, in particular, the Civil Procedures Code requires reciprocity of enforcement between the

UAE and the country issuing the judgment. Under the Civil Procedures Code, a judgment of a foreign court may be enforced in a UAE court if:

- no UAE court has jurisdiction in the dispute and the foreign court did have jurisdiction;
- the parties in relation to which the judgment was issued have been given due notice of the proceedings and were represented;
- the foreign judgment is final; and
- the judgment does not contradict any judgment issued in the UAE and contains nothing that would be in breach of public policy, order or morals.

The UAE courts have a broad jurisdiction to hear any proceeding with a UAE element. In summary, the UAE courts may assume jurisdiction if:

- a party is domiciled in the UAE;
- the claim concerns an asset that is located in the UAE;
- the claim concerns a contract under which the contractual obligation should have been or was performed, concluded, executed, completed or relevant payments were made in the UAE;
- the claim is in respect of insolvency that has been declared in the UAE;
- the claim is against a UAE national or expatriate who is domiciled in the UAE; or
- the claim concerns a party who is employed in the UAE.

We are not aware of any international treaties on insolvency having been signed by the UAE. The UAE is a signatory to the New York Convention on the Recognition and Enforcement of Arbitral Awards and has signed a limited number of treaties on the recognition of foreign judgments, including the Riyadh Arab Agreement for Judicial Cooperation (the Riyadh Convention) and the GCC Convention for the Enforcement of Judgments and Judicial Notices and Delegations (GCC Convention), which was ratified by the UAE in June 1996. Under the GCC Convention, judgments issued in any of the six member countries of the GCC (UAE, Bahrain, Qatar, Kuwait, the Kingdom of Saudi Arabia and the Sultanate of Oman) are enforceable in any other GCC country. We are not aware of any proposal to adopt the UNCITRAL Model Law on Cross-Border Insolvency.

**COMI****48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

The Commercial Code does not set out a specific test and the question of determining this has not to our knowledge been addressed and the legislation is largely untested as there has yet to be a major corporate insolvency in the UAE. In principle, the UAE courts have jurisdiction to hear bankruptcy cases relating to any commercial entity trading in the UAE that is a 'trader' conducting its principal activity in the UAE, or that has its central management in the UAE as defined in the Commercial Code. The definition of trader is very broad and, effectively, covers all commercial entities by virtue of either the form of entity or through the type of commercial activity undertaken. The bankruptcy provisions can also apply to foreign 'traders' conducting their principal activity in the UAE or which have their central management in the UAE.

**Cross-border cooperation****49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

Neither the Commercial Code nor the Civil Code provides guidance to courts or insolvency administrators in such circumstances. We are not aware of any formal cooperation processes between the UAE and foreign courts and officials in the context of insolvencies and restructurings. We are, however, aware of increasing dialogue between UAE regulators and foreign regulators and this could, depending on the circumstances, relate to insolvencies.

As noted in question 47, the UAE has not incorporated into national law the UNCITRAL Model Law on Cross-Border Insolvency and there are no provisions in the UAE law for recognition of insolvency proceedings commenced in other jurisdictions or for cooperation with the courts of other jurisdictions. The UAE courts may recognise a foreign judgment of insolvency on reciprocal basis but such recognition would be subject to a number of conditions, including compliance with public policy in the UAE, both parties having obtained adequate representation and the judgment being obtained from a jurisdiction that enforces UAE judicial rulings. As a matter of practice, however, the UAE courts will generally seek to assert their jurisdiction over any matter involving UAE parties and they are unlikely to recognise the appointment of foreign insolvency officials or proceedings without consideration of the issues independently under UAE law.

The new ADGM Insolvency Regulations do incorporate the UNCITRAL Model Law on Cross-Border Insolvency, subject to a test that the company seeking insolvency proceedings in the ADGM has a 'sufficient connection' with the ADGM. It remains to be seen how this test will be interpreted by the ADGM courts.

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**Cross-border insolvency protocols and joint court hearings**

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

We are not aware of any such cases.



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# United States

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

Title 11 of the United States Code (the Bankruptcy Code) governs insolvencies and reorganisations in the United States. A federal statute, the Bankruptcy Code pre-empts state laws governing insolvency and restructuring of debtor-creditor relationships. Two primary tests for insolvency exist under US law, however, insolvency is not required to file a voluntary petition under the Bankruptcy Code: equitable insolvency, generally defined as a debtor's inability to pay debts as they become due in the usual course of business; and balance sheet insolvency, generally defined as a financial state in which the amount of the debtor's liabilities exceeds the value of its assets. The Bankruptcy Code adopts the balance-sheet test for insolvency and defines 'insolvent' as a financial condition such that the sum of the debtor's debts is greater than all of the debtor's property at a fair valuation. The Bankruptcy Code uses the term in various provisions, including with respect to the fixing of statutory liens, reclamation rights, avoiding powers (eg, fraudulent and preferential transfers) and set-offs. Bankruptcy courts have generally adopted a flexible approach to insolvency analysis. They value companies that can continue day-to-day operations on a going concern or market price basis, and may rely on a combination of valuation methodologies. Exceptions exist to the use of the balance sheet insolvency test with respect to involuntary bankruptcy petitions and a municipality's eligibility for bankruptcy relief: in those cases, the Bankruptcy Code employs a variant of the equitable insolvency standard and only permits relief if the debtor is generally not paying its debts as they become due unless such debts are the subject of a bona fide dispute as to liability or amount.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

Bankruptcy courts preside over insolvencies and reorganisations conducted under the Bankruptcy Code. They are units of the federal district courts and have limited jurisdiction. They may only enter final orders and judgments in certain 'core' matters, that is, those that invoke a substantive right under the Bankruptcy Code or that, by their nature, could only arise in bankruptcy. In non-core matters, in the absence of the parties' consent, the bankruptcy court may only submit proposed findings of fact and conclusions of law to the district court for de novo review. A non-core matter is one that does not depend on bankruptcy law for its existence and that could proceed in a non-bankruptcy forum. The US Supreme Court has ruled that bankruptcy courts lack the constitutional authority to enter a final judgment on a state law counterclaim that is not resolved in the process of ruling on a creditor's proof of claim. As narrowly interpreted, the ruling means that, absent the parties' consent, a bankruptcy court cannot enter a final judgment on some counterclaims asserted by the estate against a creditor who files a proof of claim, but that the bankruptcy court's exercise of jurisdiction is otherwise unaffected. Courts interpreting the ruling more broadly conclude that bankruptcy courts lack constitutional authority to enter a final judgment on a much wider range of claims, including fraudulent transfer claims. Jurisprudence interpreting the US Supreme Court

opinion continues to develop. Most recently, in *Wellness International Network, Ltd v Sharif*, 135 S Ct 1932 (2015), the US Supreme Court clarified that through knowing and voluntary consent, parties may waive the right to have a non-bankruptcy court adjudicate non-core claims. Moreover, such consent can be implied, and need not be express.

The federal district court in the district in which the bankruptcy court sits hears appeals from bankruptcy court decisions, although direct appeals to the federal circuit court of appeals may be taken in certain instances. With the parties' consent, a bankruptcy appellate panel (BAP) may also hear appeals from a bankruptcy court order if one has been established in the relevant judicial circuit. Panels of three bankruptcy court judges comprise BAPs. In contrast, a single district court judge typically hears appeals to the district court. Appeals to the federal circuit courts of appeal and, ultimately, the United States Supreme Court, provide additional levels of appellate review.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

A debtor must have a domicile, residence, place of business or property in the United States to be eligible for relief under the Bankruptcy Code. Eligible debtors include corporations, partnerships, limited liability companies, other business organisations and individuals. Specialised provisions apply to municipalities, railways, stockbrokers, commodity brokers, clearing banks, family farmers and fishermen. Domestic insurance companies, most domestic banks, similar financial institutions and small business investment companies licensed by the Small Business Administration are excluded. State regulators have jurisdiction over insolvent insurance companies and state-chartered financial institutions. Federal regulators have jurisdiction over federally chartered financial institutions. The commencement of a bankruptcy case other than with respect to a municipality or an ancillary proceeding under Chapter 15, creates an estate comprising all legal or equitable interests of the debtor in property as of the commencement of the case, wherever located. The Bankruptcy Code's definition of property of the estate is very broad and includes all types of property, including tangible and intangible property, as well as causes of action. Notwithstanding the breadth of the bankruptcy estate, an individual debtor may exempt certain property from its scope, thereby excluding it from his or her insolvency proceedings and rendering it immune from the claims of most pre-petition creditors. The Bankruptcy Code prescribes minimum federal exemptions with respect to statutorily delineated items. However, a state may opt out of the federal exemptions and require individual debtors to look to the state's exemption law. State law exemptions vary. The federal exemptions are illustrative of property typically exempt under state law, and include, subject to a monetary cap that varies depending on the category of property, among others, an interest in the debtor's homestead, a motor vehicle, personal jewellery, household goods and furnishings, and tools of trade. Property exempted under either the federal or state system remains subject to certain types of claims, including non-dischargeable taxes, non-dischargeable alimony, maintenance or support obligations, and unavoidable liens.

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**Public enterprises**


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**4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?**

Chapter 9 of the Bankruptcy Code governs municipal bankruptcies. An entity may only be a debtor under Chapter 9 of the Bankruptcy Code if such entity:

- is a municipality;
- is specifically authorised in its capacity as a municipality or by name to be a debtor under such chapter by state law, or by a governmental officer or organisation empowered by state law to authorise such entity to be a debtor under such chapter;
- is insolvent;
- desires to effect a plan to adjust its debts; and
- has obtained the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;
- has negotiated in good faith with creditors and has failed to obtain the agreement of creditors holding at least a majority in amount of the claims of each class that such entity intends to impair under a plan in a case under such chapter;
  - is unable to negotiate with creditors because such negotiation is impracticable; or
  - reasonably believes that a creditor may attempt to obtain a transfer that is avoidable as a preferential transfer under section 547 of the Bankruptcy Code.

Assuming a municipality is eligible for Chapter 9 protection, the case proceeds like a Chapter 11 reorganisation case. The municipal debtor may assume or reject executory contracts, and attempts to negotiate a restructuring plan with its stakeholders. However, the standards for confirming a Chapter 9 plan and other aspects of a Chapter 9 case differ significantly from those applicable in a corporate restructuring under Chapter 11 of the Bankruptcy Code. The differences reflect congressional concern about maintaining the proper balance between the sovereign integrity of the state, on the one hand, versus the federal constitutional power to enact uniform laws on bankruptcy, on the other.

Creditors have many of the same remedies as they do in a traditional bankruptcy case. General unsecured obligations are subject to impairment and restructuring, with special provisions applicable in Chapter 9 to certain types of obligations, such as special revenue bonds. Creditors must file proofs of claim, and while an official committee of unsecured creditors is not automatically appointed, the United States Trustee has the authority to appoint committees of creditors holding similar claims to represent such interests during the case. In the end, seeking dismissal of the Chapter 9 case, if successful, serves as a creditor's strongest remedy.

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**Protection for large financial institutions**


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**5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?**

In response to the 2008 financial crisis, Congress enacted the Dodd-Frank Wall Street Reform and Consumer Protection Act (the Dodd-Frank Act) in 2010. The Dodd-Frank Act, inter alia: established a new independent agency, the Consumer Financial Protection Bureau, to protect consumers from abusive practices relating to mortgages, credit cards and other financial products; established the Financial Stability Oversight Council, made up of federal financial regulators and other financial participants, charged with identifying and responding to emerging systemic risks in the financial system; and implemented legislation to manage 'too-big-to-fail' financial institutions during times of financial stress. The regulatory reform includes creation of an orderly liquidation mechanism that allows the Federal Deposit Insurance Corporation (FDIC) to unwind failing systemically significant financial institutions (SIFIs) outside of bankruptcy. In addition, SIFIs must create 'living wills' detailing how the SIFI would plan for a rapid and orderly shutdown should the enterprise face financial failure. The Volcker Rule, also promulgated under the Dodd-Frank Act, imposes a number of trading restrictions on financial institutions in an effort to separate the investment banking, private equity and proprietary trading sections of a financial institution from its retail and consumer lending arms. The expansive Dodd-Frank Act legislates numerous other

areas of the financial system in an effort to lower and more effectively manage systemic financial risk.

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**Secured lending and credit (immoveables)**


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**6 What principal types of security are taken on immoveable (real) property?**

The mortgage constitutes the principal form of security device for real property and may extend to rents, proceeds and fixtures. Other real property security devices exist under state laws, including the deed of trust and land sale contract.

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**Secured lending and credit (moveables)**


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**7 What principal types of security are taken on moveable (personal) property?**

The security interest constitutes the principal security device taken on moveable property. Article 9 of the Uniform Commercial Code (UCC), enacted in all states, governs the creation and perfection of security interests in most goods. Other provisions of the UCC apply to security interests in intangible property. State certificates of title statute govern security devices in vehicles. Federal law governs the creation and perfection of security interests in most intellectual property and in aircraft and vessels.

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**Unsecured credit**


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**8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?**

An unsecured creditor generally has no special rights to any of the debtor's property until it obtains and enforces a judgment; commencement of a lawsuit to collect on the debt remains a creditor's principal remedy. A debt collection action may be a streamlined proceeding that gives rise to a judgment in a few months. The suit's complexity typically determines its length. Pre-judgment remedies (writs of attachment, garnishment and replevin) exist. Special procedures generally do not apply to foreign creditors, except for the enforcement of arbitration awards involving foreign creditors, which generally proceed under federal law.

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**Voluntary liquidations**


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**9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?**

Chapter 7 governs liquidation and is commenced by filing a petition in the bankruptcy court in the judicial district where the company is incorporated or has its principal place of business or assets or, in the case of an individual, where he or she has a domicile or residence. Filing the Chapter 7 petition immediately triggers the automatic stay and enjoins most creditor enforcement actions. It also creates the bankruptcy estate. A trustee is appointed, who typically displaces company's management and who may operate the debtor's business for a limited period if doing so is in the best interests of the estate and consistent with its orderly liquidation. In the case of an individual debtor, the trustee will oversee and administer the case, and will liquidate the debtor's non-exempt assets. Companies and individuals may also seek to liquidate under Chapter 11.

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**Involuntary liquidations**


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**10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?**

Creditors may file an involuntary Chapter 7 liquidation against any debtor that would be eligible to file a voluntary case that is not paying its debts, other than farmers, railways and not-for-profit corporations. In general, at least three creditors holding in aggregate unsecured claims of US\$15,325 that are not contingent as to liability or in dispute as to liability or amount, must sign the involuntary petition. If contested, the court may not order relief unless the debtor is generally not paying its debts as they become due (unless such debts are the subject of a bona fide dispute as to liability or amount), or the debtor turned its assets over to a custodian for liquidation in the 120 days before the date

of the filing of the petition. Balance sheet insolvency is not grounds for involuntary relief. The filing of an involuntary petition triggers the automatic stay. The debtor may continue to operate its business during the 'gap' period while an involuntary petition is contested, although the court may appoint an interim trustee for cause. If the court grants an involuntary petition, the case proceeds in the same manner as a voluntary Chapter 7 case and a trustee is appointed. The debtor may convert an involuntary Chapter 7 case to a voluntary Chapter 11 case to maintain control of the bankruptcy process.

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### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

Any eligible debtor who proceeds in good faith may commence a Chapter 11 case by filing a petition and paying a filing fee. A debtor need not be insolvent, either on a cash flow or balance sheet basis. The filing of a Chapter 11 petition immediately triggers the automatic stay and creates the Chapter 11 estate. A Chapter 11 debtor typically continues to operate its business as a 'debtor-in-possession'. It enjoys the exclusive right to propose a Chapter 11 plan for the first 120 days of the case, which exclusive right may be extended for cause to no more than 18 months, after which other interested parties may file their own plans.

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### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

Creditors must meet the same requirements applicable to an involuntary Chapter 7 case to commence an involuntary Chapter 11 case. If the court grants the involuntary Chapter 11 petition, the case proceeds like any other Chapter 11 case.

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### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

US law imposes no absolute obligation on a company's board to commence insolvency proceedings. The board of an insolvent company may in good faith pursue strategies to maximise the value of the company that do not involve commencement of insolvency proceedings. When a company is actually insolvent, the directors' fiduciary duties to the corporation under many states' laws expand to include the interests of creditors, as well as of shareholders. But no other consequences exist if a company carries on business while insolvent, assuming it does so in good faith and in accordance with applicable law. Courts generally view creditors in such circumstances as having sufficient protections through contractual obligations between corporations and creditors, or fraudulent conveyance law and the implied covenant of good faith and fair dealing, such that additional layers of protection are considered unnecessary.

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### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

No specific conditions apply to a debtor's ordinary course operation of its business during a reorganisation and it may do so without notice to creditors or court order. The debtor-in-possession, however, becomes an officer of the court and has a fiduciary duty to protect and preserve the assets of the estate and to administer them in the best interests of its creditors. Creditors who supply goods or services post-petition are usually paid on a current basis and, if not, have an administrative expense claim that usually entitles them to a full recovery as a condition to the debtor's emergence from Chapter 11. As discussed in

question 18, sections 363 and 365 govern the sale of assets outside the debtor's ordinary course of business.

One or more official and, often, unofficial committees and the US trustee monitor the debtor's activities during reorganisation. The court may also appoint a trustee for cause, including fraud, dishonesty, incompetence or gross mismanagement and, in certain cases, an examiner may be appointed to investigate specified matters. The court generally does not insert itself into the day-to-day management of the debtor's affairs and when court approval is required, generally defers to the debtor's business judgment. A debtor must obtain court approval for transactions not in the ordinary course; use of a secured lender's cash collateral (in the absence of its consent); compromises and settlements; and debtor-in-possession financing. The court must also approve the debtor's retention and payment of professionals.

In general, directors and officers continue to exercise their normal powers in the ordinary course after the commencement of a Chapter 11 case and a bankruptcy court will not interfere in the corporate governance of the debtor absent a showing of 'clear abuse'. Thus, the Bankruptcy Code leaves state corporate governance law largely untouched and bankruptcy courts generally do not take sides in corporate governance disputes. The primary exception is the power to order the appointment of a Chapter 11 trustee. Section 1104 of the Bankruptcy Code authorises a bankruptcy court to appoint a Chapter 11 trustee 'for cause' or 'if such appointment is in the interests of the creditors, any equity security holders, and other interests of the estate'. Courts consider a number of factors when determining whether to appoint a trustee, and doing so does not necessarily require a finding of fault. These factors include, among others: the trustworthiness of the debtor; the debtor-in-possession's past and present performance and prospects for the debtor's rehabilitation; the confidence – or lack thereof – of the business community and of creditors in present management; and the benefits derived by the appointment of a trustee, balanced against the cost of appointment. The appointment of a Chapter 11 trustee, however, remains the exception rather than the rule.

In contrast, in a Chapter 7 case, an independent trustee is appointed who displaces management. The board typically resigns. The Chapter 7 trustee's primary purpose is to collect, liquidate and distribute estate property as expeditiously as is compatible with the best interests of the parties. In rare instances, a Chapter 7 trustee may continue to operate the debtor's business for purposes of maximising its liquidation value.

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### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

The filing of a bankruptcy petition triggers an automatic stay and no formal court order need be obtained. The automatic stay is broad in scope and applies to almost all types of creditor actions against the debtor or property of its estate. The limited statutory exceptions to the stay include criminal proceedings against the debtor, enforcement of a governmental unit's police or regulatory powers, a non-debtor party's right to close out most securities and financial contracts, and certain other actions taken by specified parties.

A court may, upon a creditor's request and after notice and a hearing, grant relief from the automatic stay:

- 'for cause, including the lack of adequate protection of an interest in property' held by such creditor; or
- with respect to an action against property of the estate, if the debtor does not have any equity in such property (ie, the claims against such property exceed its value) and such property is not necessary for the debtor's effective reorganisation.

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### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

Section 364 of the Bankruptcy Code governs post-petition financing. A debtor-in-possession may obtain post-petition unsecured credit in the ordinary course of its business without court approval. Other financing requires court approval. The court may authorise unsecured post-petition credit as an administrative expense. It may also grant the

lender a 'super priority' claim that has priority over all other administrative priority and general unsecured claims, other than the payment of administrative expenses in a superseding Chapter 7 case. A debtor-in-possession may also obtain secured credit and the court may authorise a lien that is junior, senior or equal to an existing lien on the debtor's assets. Liens that are senior or equal to existing liens may be granted if the debtor demonstrates that it is unable to obtain credit otherwise, and adequate protection of the existing lienholder's interests exists. Non-consensual priming liens are rare since debtors usually cannot provide pre-petition secured lenders with adequate protection due to a lack of unencumbered cash flow and assets. Trustees in Chapter 7 cases may also obtain credit if authorised to operate the debtor's business.

#### Set-off and netting

##### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

The Bankruptcy Code generally honours a creditor's set-off right of mutual pre-petition debts and treats it like a secured claim. Courts have interpreted the Bankruptcy Code's 'mutual debt' requirement, however, as requiring a mutuality of parties, thereby rendering ineffective in bankruptcy agreements to set off amounts owed to affiliates of a counterparty ('triangular set-offs' or cross-affiliate netting), even though such agreements are enforceable under non-bankruptcy contract law. Except for set-offs arising from certain securities transactions, a creditor must obtain relief from the automatic stay prior to setting off. The Bankruptcy Code does not recognise a set-off if the creditor asserting the right acquired the claim against the debtor from another creditor either after the debtor's bankruptcy filing or within 90 days of the filing while the debtor was insolvent. Set-offs are also barred if the creditor became indebted to the debtor for the purpose of obtaining the set-off, and the creditor incurred the debt within 90 days of the debtor's filing while the debtor was insolvent. Limits also exist on recovery of certain preferential set-offs taken within the 90 days immediately preceding the debtor's filing of its bankruptcy case.

#### Sale of assets

##### 18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?

Sections 363 and 365 of the Bankruptcy Code govern the sale of assets outside the ordinary course of business (including the sale of some or all of the debtor's business), and assumption and assignment of leases and executory contracts. A debtor must support such a sale or use of property with an articulated business reason. This business judgment standard is flexible, and courts consider all salient factors pertaining to the proceeding and proposed sale when determining whether a proffered business justification satisfies the standard with respect to any particular transaction. A debtor may also sell assets or its business pursuant to a Chapter 11 plan. A purchaser typically acquires the assets free and clear of any claim or interest. Future claims, that is, claims where the injury has not yet manifested itself (typically based on product liability or similar tortious conduct), present the principal exception to this general rule and may give rise to successor liability. The Bankruptcy Code permits private asset sales as well as auctions. Auctions typically take place outside the courtroom pursuant to judicially approved sales procedures. Auctions often include a sale agreement that sets the floor for other bids - a 'stalking horse bid'. The court approves the terms of the stalking horse bid, including any break-up fee or other buyer protections. Unless the court for cause orders otherwise, the Bankruptcy Code in general permits a secured creditor to bid up to the full amount of its claim to purchase a debtor's assets during a bankruptcy case and the practice is common. The Bankruptcy Code does not define 'cause'. Courts interpret the term flexibly and apply it on a case-by-case basis. Little case law exists addressing what constitutes 'cause' to deny a secured creditor's right to credit bid. Rulings suggest

that a court will only limit a secured creditor's right to credit bid where the creditor's lien is not fully perfected, collusion exists, or allowing the original credit bid would chill the bidding process and suppress the sale price. Absent collusion or lack of good faith, the fact that the credit bidder is an assignee of the original secured creditor should not affect the assignee's right to credit bid, and the practice is common. The US Supreme Court has definitively ruled that a secured creditor has an absolute right to credit bid when a debtor sells a secured creditor's collateral under a Chapter 11 plan, rather than pursuant to section 363 of the Bankruptcy Code during the pendency of the case.

#### Intellectual property assets in insolvencies

##### 19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?

The automatic stay prevents an IP licensor from terminating the debtor's right to use the licensed intellectual property. Courts usually treat IP licences as executory contracts and a debtor may continue using the IP during its Chapter 11 case if it pays royalties and otherwise complies with the licence. A debtor's ability to assume an IP licence and continue using it after exiting from bankruptcy, or selling the IP licence to a third party, may generate controversy and depends on the nature of the licence under non-bankruptcy law.

Section 365(n) of the Bankruptcy Code protects a licensee's right to use intellectual property where the debtor is the IP licensor. Prior to rejecting an IP licence, the debtor must perform the contract, provide the licensee with the IP and otherwise not interfere with the licensee's contractual rights. A licensee may elect to retain its rights under the IP licence, as such rights existed immediately before the commencement of the bankruptcy case, notwithstanding the debtor's rejection of the IP licence if it makes royalty payments and waives any set-off and administrative claims arising under the licence.

#### Personal data in insolvencies

##### 20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?

The Bankruptcy Code restricts the ability to sell or lease estate assets if the assets include 'personally identifiable information' about non-debtor individuals, and if the debtor, in connection with offering a product or service, has in effect on the petition date a policy that prohibits transfer of such information. Personally identifiable information is broadly defined to mean information provided by an individual to a debtor in connection with obtaining a product or a service from the debtor primarily for consumer use. It includes a person's name, address, contact information, social security number, birth date and the like. In such circumstances, personally identifiable information may only be sold or leased if the sale is consistent with the debtor's policy, or if, after the appointment of a consumer privacy ombudsman, the court gives due consideration to the facts, circumstances, and conditions of the sale or lease and no violation of applicable non-bankruptcy law would ensue. The court directs the US trustee to appoint a consumer privacy ombudsman if a transaction requires doing so. The consumer privacy ombudsman is a disinterested person compensated by the debtor's estate who assists the court in its consideration of the facts and circumstances of the proposed sale or lease. Relevant information that the ombudsman may present to the court for consideration includes the impact of the transaction on the potential loss of consumer privacy, and the related potential harm and cost.

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### Rejection and disclaimer of contracts in reorganisations

#### 21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?

Upon notice and a hearing, a debtor may reject almost any pre-petition executory contract or lease other than a collective bargaining agreement, which it may only reject or modify in compliance with section 1113 of the Bankruptcy Code. A debtor may also not unilaterally reject or fail to pay retiree insurance benefits; these may only be modified or rejected in compliance with section 1114 of the Bankruptcy Code. The rejection of a contract is deemed a pre-petition breach that gives rise to an unsecured claim for damages. Rejection of the contract relieves the debtor and non-debtor party to the contract of continued performance.

Where a debtor's obligations stem from pre-petition contractual liability, even a post-petition breach will be treated as a pre-petition liability if the debtor elects to reject the agreement. When a debtor elects to assume a contract, it is required to cure any defaults including amounts owed on account of post-petition breaches. Where a debtor-in-possession elects to continue to receive benefits from the non-debtor contract counterparty to an executory contract pending a decision to assume or reject the contract, the debtor-in-possession is obligated to pay for the reasonable value of those services. Thus, claims of contract counterparties who are induced to supply goods or services to a debtor-in-possession pursuant to a contract that has not been rejected are afforded administrative priority to the extent that the consideration supporting the claim was supplied during the reorganisation.

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### Arbitration processes in insolvency cases

#### 22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?

Federal law and courts strongly favour the use of alternative dispute resolution, and arbitration procedures are employed in bankruptcy cases, although mediation is more commonly used. A court has the discretion to deny arbitration over a core matter integral to the bankruptcy case. The automatic stay enjoins arbitrations commenced prior to the bankruptcy filing from continuing against a debtor, although courts may grant relief from the stay to permit the proceeding to continue and often do so. Disputes that arise in an insolvency case after it is filed, most commonly relating to claims adjudication, may also be subject to arbitration or mediation and bankruptcy courts have the authority to direct parties to submit to such procedures. Large, complex Chapter 11 cases (eg, *Lehman Brothers Holdings Inc*) not infrequently employ court-approved alternative dispute resolution procedures tailored to address the specific exigencies of the case. No types of insolvency disputes exist that are categorically exempt from arbitration and mediation. Indeed, bankruptcy courts may appoint a mediator to facilitate confirmation of a reorganisation plan. In some cases a party may waive its right to arbitration if, for example, it engages in protracted litigation that prejudices the opposing party. Waiver of arbitration, however, is not lightly inferred and remains the exception rather than the rule.

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### Successful reorganisations

#### 23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?

Confirmation of a plan requires, among other things, that the Chapter 11 plan:

- be proposed in good faith and not by any means forbidden by law;
- designate all claims and interests into classes (such that all claims or interests in a particular class must be substantially similar);
- specify the treatment of each class of claims or interests and state whether such classes are impaired or unimpaired;

- include, if at least one class of claims is impaired by the plan, at least one accepting class of impaired claims (determined without including any acceptances by insiders);
- provide adequate means for the plan's implementation;
- be 'feasible' (ie, not likely to be followed by the need for liquidation or another financial reorganisation); and
- with respect to each impaired class of claims or interests, provide that each holder of a claim or interest in such class either has voted to accept the plan or will receive or retain under the plan on account of such claim or interest, property of a value as of the effective date of the plan that is not less than the amount that such holder would receive or retain if the debtor were liquidated under Chapter 7 of the Bankruptcy Code.

Known as the 'best interests of creditors test', this last requirement ensures that creditors and interest holders who do not vote in favour of the plan receive at least as much under the plan as they would receive if the debtor were liquidated under Chapter 7. Unimpaired classes are classes whose claims are reinstated or paid in full as if the bankruptcy had not occurred. They are deemed to have accepted the plan and are not entitled to vote on the plan. Conversely, classes that receive no distribution under the plan, likewise, are not entitled to vote because they are deemed to have rejected the plan.

Holders of impaired claims or interests may vote to accept or reject a plan. A class of claims is deemed to accept a plan if such plan has been accepted by creditors that hold at least two-thirds in amount and more than half in number of the allowed claims of such class held by creditors that have voted. A class of interest holders accepts a Chapter 11 plan if holders of in excess of two-thirds of the number of shares actually voting accept the plan.

If an impaired class rejects a plan, the plan may be confirmed only through 'cram down'. Cram down requires, along with the requirements above, that the plan does not 'discriminate unfairly' and be 'fair and equitable' with respect to each impaired, non-accepting class. To avoid unfair discrimination, a plan must classify similarly situated claims together and treat them similarly. The 'fair and equitable' standard strives to respect the existing priorities of claims and interests (the 'absolute priority rule') so that senior claims in dissenting classes must be satisfied in full before junior claims or interests can receive or retain any property under the plan.

While debtors may in appropriate circumstances release others, courts remain divided over whether a plan may include releases by creditors and other parties in interest in favour of non-debtors. Such releases are permitted only in unusual circumstances, if at all. At a minimum, third-party releases must be necessary and fair. A plan may, however, contain releases and exculpations in favour of the debtor's officers, directors, advisers and other professionals, as well as statutory committees and their advisers, and in appropriate instances other key stakeholders who provided substantial consideration to the reorganisation (including lenders) and their advisers, for acts and omissions made in connection with or arising from the Chapter 11 case itself.

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### Expedited reorganisations

#### 24 Do procedures exist for expedited reorganisations?

The Bankruptcy Code specifically authorises expedited reorganisations and permits prepackaged plans that a debtor negotiates and in respect of which it solicits votes prior to filing for Chapter 11 relief. A debtor may also file a 'pre-arranged' Chapter 11 case in which it negotiates pre-Chapter 11 the terms of its reorganisation with major creditor constituencies but does not solicit votes in favour of a plan until after the Chapter 11 filing.

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### Unsuccessful reorganisations

#### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

A Chapter 11 plan must meet the confirmation requirements described in question 23. Failure to confirm a Chapter 11 plan provides grounds for dismissal or conversion of the case to a liquidation under Chapter 7. A court may also permit the filing of an alternative plan. Material default under a confirmed plan or inability to substantially consummate a confirmed plan constitute grounds for dismissal or conversion to

liquidation under Chapter 7. The court may give a plan proponent the opportunity to cure a default under a confirmed plan. A debtor may also modify a plan after its confirmation and before its substantial consummation if the modified plan meets the requirements for confirmation.

### Insolvency processes

**26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?**

Creditors receive notice of most significant aspects of a liquidation or reorganisation case, including: case commencement; the bar date for filing claims; dates for the meeting of creditors; any proposed sale, use or lease of property outside of the ordinary course of business; the deadline to vote on a plan; and fee applications of professionals. Shortly after a case is filed, the US trustee convenes a meeting of creditors at which they may examine the debtor. On motion of any party in interest, the court may also order the examination of any entity, including the debtor. Numerous reporting obligations exist. A debtor (or trustee) must file operating and financial reports that disclose the debtor's business and financial performance while in bankruptcy. A debtor also has a duty to keep records of receipts and disposition of assets, and in a Chapter 11 case, report financial information concerning entities in which the debtor holds a controlling interest. Without court approval, creditors and official committees cannot initiate an action against a third party on account of a claim that is property of the debtor's estate or that belongs to the debtor. A plan may provide for non-consensual releases of non-debtor third parties in most jurisdictions. Such releases, however, are the exception, not the rule, and courts only grant them in extraordinary circumstances.

### Enforcement of estate's rights

**27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

The court may grant a creditor or, more often, a creditors' committee, derivative standing to pursue actions on behalf of the debtor or its estate, but litigation proceeds generally inure to the benefit of the estate. Alternatively, the trustee may retain an attorney on a contingency fee basis under which the attorney receives a fixed percentage of any recovery, with the excess reverting to the debtor's estate. With court approval, a debtor's secured lenders or others may fund the debtor's prosecution of a valuable estate claim for the benefit of the estate generally.

### Creditor representation

**28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

In Chapter 11 cases, the US trustee must appoint a committee of creditors holding unsecured claims and may appoint additional committees (eg, to represent equity holders, mass tort claimants or employees). Five to seven creditors, selected from the debtor's 20 largest creditors and who have indicated a willingness to serve, usually comprise a statutory committee. Statutory creditors' committees serve as fiduciaries for unsecured creditors generally and perform an oversight function. They may investigate the debtor's acts, conduct, assets, liabilities, financial condition, business operations and any other matter relevant to the case or to the formulation of a plan. Subject to court approval, a creditors' committee may retain attorneys, financial advisers and other professionals. The debtor pays their approved fees and expenses.

Unofficial (or ad hoc) committees, including committees of secured (or undersecured) lenders, equity holders, noteholders and trade creditors, may also play an important role in reorganisations. Ad hoc committees are self-appointed and self-regulated. Like other interested parties, they have standing to be heard on most issues in a case, may file motions, and may otherwise appear before the court and participate in

the restructuring process. Ad hoc committees routinely retain attorneys and financial advisers. The debtor may be required to pay an ad hoc committee's professional fees and expenses if the court finds that the committee made a 'substantial contribution' to the case, or if a Chapter 11 plan so provides, although the latter is subject to some debate.

### Insolvency of corporate groups

**29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

A court may consolidate the cases of two or more affiliated debtors pending in the same court for administrative purposes and almost always does so. Courts have the power to combine the assets and liabilities of companies into one pool for distribution purposes under the equitable doctrine of substantive consolidation. A proponent of substantive consolidation must generally show some form of substantial identity between the entities to be consolidated and that consolidation is necessary to avoid some harm or to realise some benefit. Courts view substantive consolidation as an extraordinary remedy that should be used sparingly if an objection is lodged. In cases involving jointly administered corporate groups, the court may in appropriate circumstances authorise the use of cash and other assets by non-debtor affiliates (including those located outside the United States), typically with the secured creditors' consent. In addition, Chapter 15 of the Bankruptcy Code authorises the court, upon recognition of a foreign proceeding, to entrust the administration or realisation of all or part of the debtor's assets within the territorial jurisdiction of the United States to a foreign representative. The court may also entrust the distribution of all or part of the debtor's assets located in the United States to the foreign representative for administration in the foreign proceeding, provided that the court is satisfied that the interests of creditors in the United States are sufficiently protected.

### Appeals

**30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

A party may appeal a final order of the bankruptcy court as of right, and may appeal an interlocutory (or non-final order) with leave of the court. A decision is final if it ends the litigation on the merits, and leaves nothing for the court to do but execute the judgment. An interlocutory order only decides some discrete matter pertaining to the case, and requires additional steps for full adjudication. District courts generally adopt a flexible approach to the concept of finality in the bankruptcy context, recognising that, unlike a traditional civil case, a bankruptcy case may give rise to numerous discrete disputes that could be finally adjudicated for purposes of an appeal.

Appeals of interlocutory orders require the filing of a motion for leave to appeal in addition to the filing of a notice of appeal. District courts may review an interlocutory order if:

- the order involves a controlling question of law as to which there is substantial ground for difference of opinion; and
- immediate appeal from the order may materially advance the ultimate termination of the litigation or advance the bankruptcy proceedings.

However, granting leave to file interlocutory appeals in bankruptcy cases is the exception, not the rule; interlocutory appeals are disfavoured because of the disruptive effect such appeals generally have on the bankruptcy process and a debtor's restructuring efforts. Federal circuit courts of appeal, in contrast to district courts, generally only have jurisdiction over final orders. Appeals of bankruptcy matters to the US Supreme Court also do not proceed as of right, and are granted in the Court's discretion.

An appellant does not need to post security or a bond to proceed with an appeal unless the appellant seeks a stay of the order of the bankruptcy judge pending appeal. Posting security in the form of a bond

protects the prevailing party against any loss that might result from a stay of the order. In determining whether a bond should be required, a court will focus on whether the bond is necessary to protect against any reduction in value of the subject property pending appeal, and to secure the prevailing party against any loss that might be sustained as a result of an ineffectual appeal. Courts have the discretion to grant a stay pending appeal without requiring the appellant to post a bond. Because a bond is meant to protect the non-moving party from the potential harm of a stay, courts consider a number of factors when sizing the amount of the bond in bankruptcy cases. Where a movant seeks to stay an appeal of a court order confirming a Chapter 11 plan, for example, the potential harm caused by the stay may be the diminishing value of the entire Chapter 11 estate occasioned by the stay. In such cases, the potential harm could be substantial, and courts have required bonds over US\$1 billion. As a practical matter, this effectively denies the stay of the order, as few parties have the funds (or appetite to risk) such amounts.

### Claims

**31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

A debtor lists all known claims in its schedules of assets and liabilities and classifies them as 'disputed', 'unliquidated' or 'contingent' where appropriate. A Chapter 11 debtor usually obtains a court order setting a bar date by which creditors must file proofs of claim, however, if the claim is scheduled in the proper amount and not as disputed, unliquidated or contingent, no proof of claim need be filed in a Chapter 11 case. In Chapter 7 cases, a claim is timely if it is filed no later than 90 days after the first date set for the section 341 creditors' meeting, unless the case is a 'no asset' case in which the claim deadlines may be deferred. Creditors may object to a debtor's characterisation of their claim, and a debtor may object to a creditor's proof of claim. Parties adjudicate a claim dispute before the court. Non-bankruptcy law determines its validity, although the Bankruptcy Code governs the allowance of the claim in bankruptcy and sometimes trumps non-bankruptcy law rights, for example, by disallowing an unsecured creditor's claim for interest accruing post-petition and limiting a landlord's lease rejection damages to a percentage of remaining lease payments. Bankruptcy court orders disallowing a claim may be appealed. In addition, a court may for cause reconsider a claim that has been allowed or disallowed. The Bankruptcy Code defines 'claims' broadly and, as a result, claims for contingent or unliquidated amounts can be recognised and discharged. Courts must estimate contingent or unliquidated claims for purpose of allowance if the fixing or liquidating of the claim would unduly delay the administration of the case. The goal of estimation is to reach a reasonable valuation of the claim as of the date of the bankruptcy filing. The court may estimate contingent or unliquidated claims under whatever method it finds best suited to the particular exigencies of the case, but in determining the amount of the claim, is generally bound by the applicable non-bankruptcy substantive law governing the claim (eg, claims based on alleged breach of contract are estimated under accepted contract law principles). An active and well-developed claims market exists. In the absence of a court order, parties may freely transfer bankruptcy claims and the applicable rules have essentially rendered the sale of claims a private transaction between buyer and seller mostly free from court interference. For claims not based on publicly traded securities, the Federal Rules of Bankruptcy Procedure require a transferee to file evidence of the transfer of a claim, typically in the form of an assignment of claim. Any objection to the transfer must be filed within 21 days of the mailing of the notice to the transferor. In the absence of an objection, the transfer is valid. A claim acquired at a discount is enforced for its full face value, and not the discounted purchase price, if the claim is otherwise valid. An exception to this rule is bond debt acquired with an original issue discount, a portion of which may be treated as unmatured post-petition interest. The Bankruptcy Code disallows claims for unmatured post-petition interest unless the creditor claiming the interest is a secured creditor the value of whose security exceeds its claims, or the estates are solvent and can pay unsecured claims in full.

### Modifying creditors' rights

**32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?**

The court may change the treatment of creditors' claims through equitable subordination, recharacterisation and substantive consolidation. Equitable subordination lowers the priority of a creditor's claim by subordinating it to similarly situated claims upon a showing of wrongful conduct by the claim holder that damaged other creditors. Recharacterisation involves the allowance of a claim based on its economic substance rather than form. A court may recharacterise a debt claim as an equity interest if the purported claim lacks the usual attributes of indebtedness and otherwise functions like equity. As noted above, a court may 'substantively consolidate' estates. By pooling the assets of, and claims against, two or more entities, substantive consolidation may eliminate any structural priority between the claimants of the consolidated entities. Finally, at least some courts have held that they also have the power to disallow claims on equitable grounds in 'rare' cases.

### Priority claims

**33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?**

The major non-employee related unsecured claims entitled to priority in both liquidations and reorganisations are:

- expenses of administering the debtor's estate, along with judicial fees and costs;
- the value of any goods received by the debtor within 20 days before the filing of the case, which goods have been sold to the debtor in the ordinary course of the debtor's business;
- claims arising during the 'involuntary gap period' from the time an involuntary petition is filed to the time the court enters an order granting the requested relief;
- subject to a statutory cap, claims for certain kinds of consumer deposits;
- claims for taxes and customs duties and related liabilities assessed within a certain pre-petition time frame; and
- claims for depository institution capital-maintenance commitments.

Apart from priming liens approved in connection with debtor-in-possession financing, only claims relating to the debtor's preservation or disposition of a secured creditor's collateral, to the extent of any benefit to the secured creditor, are entitled to priority over a secured creditor's lien.

### Employment-related liabilities in restructurings

**34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?**

In general, applicable non-bankruptcy law determines the existence of any employee claims, regardless of whether the employee is terminated before or during a reorganisation or liquidation case, and no special bankruptcy procedures exist. For example, an employee may have a claim for unpaid severance if he is terminated before or during a bankruptcy case, and applicable contract and labour law determines the amount of his claim although the Bankruptcy Code imposes a one-year cap on damages arising from rejection of an employment contract. Similarly, non-bankruptcy labour law, including the federal WARN Act, may impose damages or fines on a company for terminating large numbers of employees without adequate notice, and bankruptcy recognises such claims. Whether a particular mass lay-off triggers any such claim depends on the facts and circumstances of the particular case, as well as on the applicable labour statutes (which vary from state to state). Subject to a statutory cap, the Bankruptcy Code affords priority in payment to an employee's pre-petition claims for wages, salaries and commissions (including holiday, severance and sick leave) earned by an individual within 180 days of a bankruptcy filing. In addition, employee wages earned post-petition, or claims that arise post-petition, are generally considered administrative expenses and entitled to payment in full to the extent earned or accrued post-petition. As discussed further

in question 35, special provisions exist for terminating collective bargaining agreements and qualified registered employee pension plans and for modifying certain retiree benefits. Very generally, a debtor may not unilaterally amend or terminate such obligations unless, among other things, it can demonstrate that the modification or termination is necessary to permit the debtor's reorganisation.

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### **Pension claims**

#### **35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

Most private-sector pension plans are governed by federal statute: the Employee Retirement Income Security Act (ERISA). ERISA requires, inter alia, certain minimum funding levels for qualified registered employee pension plans. The Pension Benefit Guaranty Corporation (PBGC) is the federal agency responsible for enforcing ERISA and for managing the mandatory government insurance programme that protects covered pensions. Under ERISA, a bankruptcy court may only approve a debtor's termination of an ERISA-covered plan if, absent such termination, the debtor will be unable to pay all of its debts pursuant to a plan of reorganisation and will be unable to continue in business outside the Chapter 11 reorganisation process. In addition, section 1113 of the Bankruptcy Code provides the exclusive means by which a Chapter 11 debtor can assume, reject or modify a collective-bargaining agreement, including any additional pension-related obligations such an agreement may impose.

If a debtor terminates an ERISA-governed pension plan in bankruptcy, the PBGC may participate as a creditor holding claims for both the amount of any underfunding as well as any unpaid contributions. Outside of bankruptcy, a statutory lien arises in favour of the PBGC for unpaid mandatory plan contributions and underfunding. In bankruptcy, the automatic stay precludes imposition of these liens and the PBGC's claims for withdrawal liability or unpaid pension plan contributions are therefore generally considered pre-petition unsecured claims and afforded no special treatment. Some courts, however, have afforded administrative expense treatment to the portion of the PBGC's underfunding or withdrawal liability claims that are attributable to the employees' post-petition labour. Unpaid pension contributions incurred post-petition but prior to plan termination may also be treated as administrative expense priority claims, although the law remains unsettled on this issue. Finally, section 507(a)(5) of the Bankruptcy Code grants priority to claims up to a limited statutory cap for pre-petition contributions to employee benefit plans.

Unlike private-sector pensions, public pensions (ie, those sponsored by states or municipalities) are governed by state and local law, not ERISA. Many states treat public pension benefits as constitutionally protected, which severely limits the public employer's ability to reduce or modify public pension benefits both inside and outside of bankruptcy. A municipality eligible to file for bankruptcy under Chapter 9 of the Bankruptcy Code, however, may have some ability to modify its pension obligations through the leverage gained by imposition of the automatic stay and the ability to assume and reject executory contracts, although the effectiveness of Chapter 9 for these purposes remains largely untested.

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### **Environmental problems and liabilities**

#### **36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

A debtor in bankruptcy must comply with all applicable environmental laws and regulations – and the exercise of the government's police power through such laws and regulations – while operating during and after bankruptcy. This means that a company that owns environmentally contaminated property cannot use bankruptcy to cleanse itself of its obligations related thereto. It must remediate the property in accordance with applicable laws, regulations, consent decrees, judgments and similar requirements. Likewise, bankruptcy does not empower an owner-operator of contaminated property to escape owner-operator liability after emerging from bankruptcy. As further discussed in

question 37, the extent to which environmental obligations otherwise can be discharged in bankruptcy remains hotly contested and has generated inconsistent and often conflicting case law. While no clear lines can be drawn, as a very general matter, claims by the government and potentially responsible third parties to recover the cost of remediation work on sites formerly owned by the debtor, and fines and penalties for pre-filing violations of regulatory requirements, are the environmental obligations most susceptible to discharge in bankruptcy. Environmental obligations associated with properties owned during and after bankruptcy, in most cases, cannot be discharged. Whether such claims travel with the assets, or can be asserted against successor entities or third parties, depends on the facts of the individual case and the outcome remains uncertain. In general, however, absent criminal conduct, the debtor's officers and directors are not held personally liable for environmental remediation claims.

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### **Liabilities that survive insolvency proceedings**

#### **37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

Confirmation of a Chapter 11 reorganisation plan generally discharges a business debtor of all its pre-petition debts to creditors. However, a plan that provides for the liquidation of all, or substantially all, of the property of the estate when the debtor does not engage in business after consummation of the plan, does not result in a discharge. A business debtor likewise does not receive a discharge in a Chapter 7 case. Upon completion of a Chapter 7 or liquidating Chapter 11 case, however, only a corporate shell remains against which claims could be satisfied. Bankruptcy discharges most debts of individual debtors with certain statutory exceptions.

A debtor may also be unable to discharge responsibility for environmental contamination obligations through the bankruptcy process. The question turns on whether a particular environmental clean-up obligation constitutes a 'claim' as defined by the Bankruptcy Code, or alternatively, a form of injunctive relief that cannot be reduced to a 'right to payment'. Environmental liability that constitutes a 'claim' (eg, a regulatory fine or claim for reimbursement) may be discharged, but other types of remedial obligations (eg, where a debtor must take action to ameliorate ongoing pollution regardless of cost to the debtor) may not. The distinction often proves unclear and courts have struggled with the conflicting aims of US bankruptcy and environmental laws in this area, resulting in inconsistent case law. Recent decisions suggest a trend towards favouring environmental over bankruptcy goals, with some courts concluding that where the government brings an action for injunctive relief against a company under an environmental protection statute that does not authorise any form of monetary relief, the obligation with respect to such injunctive relief is not a 'claim', and the company therefore cannot discharge its remediation obligations through bankruptcy.

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### **Distributions**

#### **38 How and when are distributions made to creditors in liquidations and reorganisations?**

A Chapter 11 plan specifies the time and manner of distributions. A Chapter 7 trustee generally does not make distributions until he or she has liquidated estate assets, including completion of litigation. Interim distributions may be made if sufficient liquid assets exist. Payment on account of administrative or priority claims, like wage claims or fully secured claims, may be made during the pendency of the case with court approval.

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### **Transactions that may be annulled**

#### **39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Preferential, fraudulent and post-petition transfers made without necessary court authorisation may be avoided. Broadly, a preferential transfer is one made within 90 days before the commencement of the case (or one year if to insiders) on account of antecedent debt that results in the recipient receiving a greater recovery than it would have received if the transfer had not been made and the debtor were liquidated in a Chapter 7 case. In general, a fraudulent transfer is:

- any transfer of the debtor's property, or any obligation incurred by the debtor, that was made with the 'actual intent to hinder, delay, or defraud' present and future creditors; or
- any transfer made or obligation incurred for less than reasonably equivalent value while the debtor was insolvent, thereby rendered insolvent, had unreasonably small capital to operate its business, intended or believed that it would incur debts beyond its ability to pay as they matured, or made to an insider if certain other circumstances exist.

The Bankruptcy Code's fraudulent transfer provision has a two-year reach-back period but the Code also permits use of longer reach-back periods available under state law, which typically range from four to six years. The Bankruptcy Code permits the recovery of the property transferred, or its value. The Code also disallows any claim by a transferee against the estate unless the transferee disgorges any avoided transfer for which the court finds it liable. If the transferee returns the avoided transfer, it receives a pre-petition general unsecured claim as compensation.

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### Proceedings to annul transactions

- 40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

Transfers made within the time frames specified in question 39 may be avoided. Only a debtor-in-possession or a trustee has standing to pursue an avoidance action, unless the court expressly grants creditors or a committee derivative standing to do so. Avoidance actions are available in reorganisations and liquidations.

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### Directors and officers

- 41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

If officers and directors comply with corporate law formalities, they are generally not liable for the debts and liabilities of the corporations they serve. Liability may arise on a corporate veil piercing theory. An officer or director who is a 'control person' may also be liable for certain state and federal payroll taxes that were not withheld and paid over to taxing authorities. Similarly, corporate directors and officers do not have personal liability for pre-bankruptcy actions unless they are found to have breached their fiduciary duties. Generally, no fiduciary obligations to creditors exist. Creditor rights are governed by contract, statute and case law concerning debtor-creditor relationships. Upon insolvency (or near insolvency), the directors' and officers' fiduciary obligations to the corporation may expand to take into account the interests of creditors who, upon insolvency, become the residual risk-bearers in the enterprise; however, state law is not necessarily consistent or fully developed with respect to such matters. As in all situations, directors and officers may be criminally prosecuted for fraud, securities law violations and other crimes related to the conduct of the business. Mere insolvency, or operating a company while insolvent, however, does not give rise to liability.

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### Groups of companies

- 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?**

In general, absent a contractual agreement to the contrary (eg, a guarantee), a parent or affiliated corporation is not responsible for the liabilities of its subsidiaries or affiliates. Exceptions exist under certain statutes, which impose direct liability on parent companies for the actions of their subsidiaries on principles of indirect operator liability, where a parent exercises direct and pervasive control over its subsidiary, common ownership, agency and veil piercing. These statutes include federal environmental, pension, labour and anti-foreign corrupt practices laws, inter alia. In addition, US common law recognises exceptions to the default rule of limited corporate liability under various

equitable theories known as 'alter ego', 'piercing the corporate veil' or 'single business enterprise'. While the exact standards for these equitable remedies vary, in general, a court may ignore the separateness of corporate entities and impose liability on parent or affiliated corporations within the same enterprise group when three factors exist: dominion and control by one corporation over another, improper conduct or purpose and harm or loss caused by the misuse of the corporate form. Common fact patterns for invoking these principles include the use of a corporate entity to defraud creditors, evade existing obligations, circumvent a statute or perpetuate illegal acts. Finally, commercial tort principles may expose corporate group members to extra-contractual claims arising from otherwise entity-specific contracts (eg, a lender seeks to hold a controlling parent liable for the false and misleading statements of its subsidiary borrower). A court routinely administers the bankruptcy cases of affiliated corporate debtors jointly. However, absent substantive consolidation (discussed in question 29), the court cannot distribute group company assets pro rata without regard to the assets and liabilities of the individual corporate entities involved. In practice, when formulating distributions to stakeholders under a jointly administered Chapter 11 plan, financial advisors model the distributive value allocable to each legal entity within a corporate group based on the assets and liabilities of each entity.

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### Insider claims

- 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?**

In bankruptcy, a party may be an 'insider' if the party either meets the statutory definition of insider (which includes, in the case of a company, 20 per cent voting equity holders, the debtor's directors, officers, general partner, persons in control, an affiliate or insider of an affiliate as if such affiliate were the debtor, managing agents, and relatives of same); or has such a close relationship with or control over the debtor so as to render transactions with the debtor not at arm's length. Claims by insiders are not per se invalid; however, because transactions with insiders are by their nature not arm's-length transactions, and accordingly, give rise to the fear that insiders might receive more favourable treatment or superior terms at the expense of general creditors, courts subject insider claims and transactions to heightened scrutiny. Insider claims are thus more likely to be recharacterised as equity or equitably subordinated and courts factor the insider nature of a claim into the equitable subordination and recharacterisation analysis. Similarly, rather than relying on the business judgment standard, courts subject sales to and transactions with insiders to heightened scrutiny when determining whether the transaction is fair to a debtor and its stakeholders. In some cases involving insider sales, a court may appoint an independent examiner to vet the process. Along with having their claims and transactions subject to heightened scrutiny, insider votes are not counted for purposes of determining whether at least one impaired class of claims has voted to accept a Chapter 11 reorganisation plan. Finally, the look-back period for insiders during which transfers may be subject to avoidance as preferential is longer than for non-insider creditors, and transfers or obligations incurred to or for the benefit of an insider may be avoided as constructively fraudulent if the debtor received less than reasonably equivalent value in exchange and made the transfer or incurred the obligation under an employment contract and not in the ordinary course of business, regardless of the debtor's solvency at the time. Under some state fraudulent transfer laws that include good faith as an element of a non-avoidable transfer, courts have held that transfers to insiders during the suspect period per se lack good faith, and accordingly, can be avoided as constructively fraudulent if the other elements of the statute are also satisfied.

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### Creditors' enforcement

- 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?**

Article 9 of the UCC permits a secured party to repossess collateral by self-help when it can be done without breach of the peace. Disposition of the collateral may be by public or private sale. Every aspect of the disposition must be commercially reasonable. In practice, court

### Update and trends

While no clear, unifying trend has emerged during the past year, courts have issued several interesting decisions relating to restructuring matters.

The US Supreme Court held that the US territory of Puerto Rico could not legislate around its exclusion from bankruptcy relief. Puerto Rico is struggling with over \$72 billion in debt, but cannot file for Chapter 9 relief under the Bankruptcy Code because it falls outside the statutory definition of 'municipality'. Chapter 9 of the Bankruptcy Code governs relief for, and is only available to, municipalities.

Notwithstanding its exclusion from Chapter 9, Puerto Rico enacted a law to restructure \$26 billion of utility-related debt. When challenged by utility creditors, the US Supreme Court found that Puerto Rico's restructuring law was pre-empted by the Bankruptcy Code, and that only Congress – not a US territory – was authorised to enact bankruptcy laws.

Also of interest is that the US Supreme Court has agreed to hear an appeal next term regarding the use of 'structured dismissals' to resolve bankruptcy cases. Contrary to the typical paths of resolving bankruptcy cases – Chapter 11 plan confirmation, Chapter 7 liquidation, or outright dismissal – stakeholders have used structured dismissals to distribute estate assets to creditors by incorporating provisions to that effect in dismissal orders. Through such provisions, debtors have dismissed cases and distributed residual estate assets to junior creditors in alleged violation of the Bankruptcy Code's priority and confirmation requirements. Critics have argued that structured dismissals effectively give debtors the benefit of a reorganisation without having to comply with applicable statutory standards.

Another issue of note includes a growing split among the judicial circuits regarding the scope of the 'safe harbour' in section 546(e) of the Bankruptcy Code for certain securities-related payments. This provision limits a debtor's ability to recover through avoidance actions transfers made in connection with a securities contract through financial intermediaries. Some courts have interpreted the section broadly to immunise from avoidance almost any eligible transfer made to or through a financial intermediary. The Court of Appeals for the Seventh Circuit, however, recently ruled that section 546(e) does not apply to transfers that are simply conducted through a financial institution (or other entity section 546(e) lists) if such entity acts merely as a conduit. Courts are also not in agreement on whether the safe harbour bars suits filed by or on behalf of individual creditors after plan confirmation, or rather, applies to all avoidance actions that a debtor in bankruptcy could bring.

The *General Motors* Chapter 11 cases generated a significant ruling on the scope of 'free and clear' sale orders issued under section 363 of the Bankruptcy Code. General Motors restructured through a sale of substantially all of its assets to reorganised General Motors (referred to as 'New GM') 'free and clear' of legacy liabilities, ostensibly including personal injury claims arising from allegedly defective ignition switches that General Motors installed in cars years before it filed for bankruptcy. Plaintiffs initiated class action lawsuits against New GM asserting successor liability claims and seeking damages for losses and injuries arising from the ignition switch defect. New GM argued that the claims were barred because of the 'free and clear' sale order, and could only be asserted against the Chapter 11 estates remaining after the sale, not against the reorganised debtors (New GM). On appeal, the Court of Appeals for the Second Circuit considered the extent to which a bankruptcy sale could be free from claims based on prepetition conduct that did not result in detectable injury at the time of the bankruptcy filing, and as a result, did not at that time result in any tortious consequence to a victim. The court affirmed the broad scope of 'free and clear' sale

orders and that a debtor could sell assets free and clear of such claims. However, contingent creditors of this kind nonetheless had a constitutional right to due process, the absence of which precluded application of the statutory protections. In *General Motors*' case, the court affirmed the bankruptcy court's holding that the personal injury plaintiffs were known creditors because General Motors knew or should have known about the ignition switch defect. As a result, General Motors' publication notice to such creditors did not satisfy due process, and the claims were not barred against New GM for this reason.

Courts are also addressing issues raised by the recent spate of energy-related bankruptcy cases. In particular, exploration and production debtors have sought to reject burdensome energy-gathering agreements, hoping to free themselves to renegotiate better contractual terms. Opposing counterparties have argued that under applicable state law, gathering agreements are covenants that run with the land, and, as such, are immune from rejection. Resolution of such disputes will likely require a formal adversary proceeding that affords the counterparty with greater procedural protections.

Finally, Chapter 15 filings remain steady and courts for the most part routinely grant recognition in favour of foreign proceedings. However, COMI and jurisdictional issues, among others, continue to emerge. Expanding on earlier precedent recognising that a foreign debtor's centre of main interests (COMI) may and not infrequently does change from the jurisdiction in which a foreign debtor actually did business to a 'letterbox' jurisdiction in which the foreign representative is winding up the debtor, a recent bankruptcy decision held that COMI can only change to such a jurisdiction if the foreign representative has undertaken material activities in that jurisdiction that provide a meaningful basis for the expectation of third parties. Accordingly, minimal activities by a liquidator in the foreign jurisdiction in which the foreign proceeding was commenced does not suffice to change a foreign debtor's COMI for recognition purposes. In the same opinion, the court noted that in Chapter 15, as in Chapter 11, US courts need not tolerate debtor bad faith, and that US courts had ample tools with which to address a foreign debtor's misconduct to protect creditors in the US from such bad behaviour. Separately, addressing the eligibility requirements to file for Chapter 15 relief, a bankruptcy court held that a foreign debtor with a New York choice of law and forum selection clause in a bond indenture had 'property in the United States' for filing purposes.

As the Chapter 11 case of the Baha Mar resort illustrates, however, companies with little or no nexus to the US risk dismissal of a plenary Chapter 11 case in favour of a foreign proceeding, especially if challenged by foreign creditors. The Baha Mar debtors filed for Chapter 11 based on the US incorporation of a single sales office. The remaining debtors were incorporated under Bahamian law, and the debtors' main assets (including the Baha Mar resort itself) along with the majority of their creditors, were located in the Bahamas. Moreover, a liquidation proceeding had been commenced in the Bahamas. Ruling on a motion to dismiss filed by non-US creditors, the bankruptcy court first confirmed long-standing US precedent that the cases were properly filed; that is, the debtors' minimal property in the US satisfied the eligibility requirements for Chapter 11 (or Chapter 15), and filing in the US to maintain control of the project and to reorganise, rather than liquidate, was not bad faith warranting dismissal. However, the bankruptcy court ultimately dismissed the cases in favour of the pending Bahamian proceeding, concluding that doing so was in the best interests of creditors (who had no expectation of a US filing), was consistent with principles of comity and that no greater good could be accomplished by retaining jurisdiction in the US.

proceedings are usually commenced to obtain judicial approval of the repossession and disposition of substantial assets.

### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

A corporation may dissolve or liquidate under state law. Modern corporate statutes generally provide that directors of dissolved corporations may distribute assets to shareholders only after discharging or making reasonable provision for the payment of creditors. Unlike bankruptcy, state law dissolution provides little court supervision and lacks the benefit of an automatic stay. State law procedures are also not subject to oversight by the US trustee or official creditors' committees and no collective enforcement action exists. Under state law, directors and

officers may be personally liable for unlawful distributions or the failure to adequately provide for claims, including unknown and contingent claims. In contrast, the bankruptcy process provides a centralised and judicially supervised forum for winding up a company's affairs. While more formal than state dissolution processes, bankruptcy provides greater transparency to stakeholders and ensures a greater degree of immunity for officers and directors acting on behalf of the company.

### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

In a Chapter 7 case, after all available assets have been sold and proceeds distributed to creditors, the trustee files a final report and account and certifies that the estate has been fully administered after which the court discharges the trustee and enters an order closing the case. A

Chapter 11 debtor emerges from bankruptcy protection when its confirmed plan becomes effective and it can resume operating without court oversight. Most Chapter 11 plans become effective upon their substantial consummation, that is, when:

- all or substantially all of the property proposed by the plan to be transferred has been transferred;
- the debtor or its successor has assumed management of all or substantially all of the property the plan addresses; and
- distributions under the plan have commenced.

After the Chapter 11 estate is fully administered, the court enters a final decree closing the case.

#### International cases

**47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?**

Congress adopted the UNCITRAL Model Law on Cross-Border Insolvency, with some modifications, as Chapter 15 of the Bankruptcy Code in 2005. Chapter 15 enables a foreign representative of a foreign estate to obtain US bankruptcy court recognition of the foreign proceedings and thereby access a panoply of relief with respect to the foreign debtor's assets and operations in the US, including the imposition of the automatic stay, administering the foreign debtor's US assets, and operating the foreign debtor's US business. Foreign creditors have the same rights regarding the commencement of, and participation in, a bankruptcy case as domestic creditors.

Most foreign judgments, other than those involving foreign penal and revenue laws, enjoy a strong presumption of validity in US courts. Their recognition depends primarily on principles of comity as well as state law, typically common law or the Uniform Foreign Money Judgments Recognition Act where enacted. The US is not a signatory to a treaty specifically addressing international insolvency or the recognition of foreign judgments.

#### COMI

**48 What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?**

The Bankruptcy Code does not define 'center of main interests' for purposes of recognising foreign proceedings in a Chapter 15 case. Bankruptcy courts have accordingly developed the following factors to consider when making a COMI determination: the location of the

debtor's headquarters; the location of those who actually manage the debtor (which conceivably could be the headquarters of a holding company); the location of the majority of the debtor's creditors or a majority of the creditors who would be affected by the case; the jurisdiction whose law would apply to most disputes; and the expectations of third parties with regard to the debtor's COMI.

Chapter 15 also does not specifically address corporate groups. In the US, some bankruptcy courts rely on a corporate group's 'nerve centre' when determining the subsidiary's COMI in the context of multinational corporate group insolvencies. The term 'nerve centre' derives from the US federal courts' description of the factors that determine where a corporation has its 'principal place of business' for purposes of diversity jurisdiction under US law. Under that test, where a corporation is engaged in far-flung and varied activities which are carried on in different states, its principal place of business is the nerve centre from which it radiates out to its constituent parts and from which its officers direct, control and coordinate all activities without regard to locale, in the furtherance of the corporate objective. The test applied is thus that place where the corporation has an 'office from which its business was directed and controlled' – the place where 'all of its business was under the supreme direction and control of its officers'. The 'nerve centre' approach has not been universally adopted by bankruptcy courts nationwide, however, and the law concerning determination of a corporate group's COMI for Chapter 15 purposes likely will continue to evolve.

#### Cross-border cooperation

**49 Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?**

Chapter 15 of the Bankruptcy Code directs the bankruptcy court and the trustee, or other person, including an examiner, to 'cooperate to the maximum extent possible' with a foreign court or foreign representative. In addition, the bankruptcy court or trustee may communicate directly with, or request information or assistance from, a foreign court or foreign representative. Chapter 15 of the Bankruptcy Code lists forms of cooperation that may occur between the US court or trustee and the foreign court, including the appointment of a person or body to act at the direction of the court, communication of information by any appropriate method, coordination of the administration and supervision of the foreign debtor's assets and affairs, approval or implementation of agreements concerning the coordination of proceedings and coordination of concurrent proceedings involving the same debtor.

Chapter 15 requires a bankruptcy court to enter an order recognising a foreign proceeding if three conditions are met. First, the entity applying for recognition must be a 'foreign representative' within the meaning of the statute. Second, certain procedural requirements must

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be satisfied. Finally, the foreign proceeding must be either a foreign main proceeding – that is, a foreign proceeding pending in the country where the debtor has the centre of its main interests (COMI) – or a foreign non-main proceeding – that is, a foreign proceeding, other than a foreign main proceeding, pending in a country where the debtor has an establishment. While recognition is routinely granted in the overwhelming majority of Chapter 15 cases, US courts have refused to recognise a foreign proceeding that is neither a main nor non-main proceeding.

Upon recognition, Chapter 15 mandates US courts to grant comity or cooperation to the foreign representative unless doing so would be manifestly contrary to US public policy. The exception should be construed narrowly and only invoked under exceptional circumstances concerning matters of fundamental importance for the US. Two factors generally govern application of the exception: the procedural fairness of the foreign proceeding; and whether an action taken in the Chapter 15 case would frustrate a US court's ability to administer the Chapter 15 case or impinge severely a US constitutional or statutory right. Despite the limited scope of the 'public policy' exception, a few courts have invoked the exception as grounds for denying relief to a foreign representative in a Chapter 15 case. Specifically, courts have

refused to apply foreign law as contrary to US public policy where the foreign law, unlike US law, allowed the debtor to terminate a licensee's right to use the debtor's patents; the foreign law permitted the administrator of the foreign estate to intercept the debtor's personal postal and electronic mail, a practice banned under US law and that might result in criminal liability; and the foreign law approved a restructuring plan that extinguished the guaranty obligations of the foreign debtor's non-debtor subsidiaries.

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#### **Cross-border insolvency protocols and joint court hearings**

- 50 In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?**

Bankruptcy courts routinely enter orders approving protocols for managing cross-border insolvency proceedings. US courts have a long history of communicating with courts in foreign countries and have done so with courts in countries including Brazil, Burundi, Canada, Israel, Switzerland and the United Kingdom.

# Vietnam

Thanh Tien Bui

Freshfields Bruckhaus Deringer

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## Legislation

### 1 What legislation is applicable to insolvencies and reorganisations? What criteria are applied in your country to determine if a debtor is insolvent?

#### General insolvency legislation

The legislation principally applicable to the insolvency of companies established in Vietnam is Law No. 51/2014/QH13 on Bankruptcy of the National Assembly of Vietnam dated 19 June 2014 (the Bankruptcy Law 2014). The Bankruptcy Law 2014 is largely untested. We are not aware that any high-profile bankruptcy petitions have been filed since the Bankruptcy Law 2014 came into effect on 1 January 2015.

Law No. 68/2014/QH13 on Law on Enterprises (the Enterprise Law) and its implementing regulations applies to the reorganisation or liquidation of companies in Vietnam outside of insolvency proceedings.

#### Vietnamese law generally

Vietnamese law generally is not well developed, is often vague or ambiguously drafted and does not have a system of case law precedents or other interpretative aids of binding value. This is also the case in respect of the Bankruptcy Law 2014. The law often only sets out basic principles and needs implementing regulations to be effective. Further, in part because of lack of clarity, Vietnamese law in any specific instance is subject to broad interpretation and different lawyers, governmental agencies and officials can have contrasting views on the application and interpretation. As a matter of practice, the ultimate arbiter is often the government body responsible for administering the relevant law.

#### Determining whether a debtor is insolvent

Under the Bankruptcy Law 2014, a company is considered to be 'insolvent' if it fails to repay a debt within three months from the due date.

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## Courts

### 2 What courts are involved in the insolvency process? Are there restrictions on the matters that the courts may deal with?

The People's Court at the provincial or district level in the locality where the insolvent company's registered head office is situated has jurisdiction over the bankruptcy of such company.

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## Excluded entities and excluded assets

### 3 What entities are excluded from customary insolvency proceedings and what legislation applies to them? What assets are excluded from insolvency proceedings or are exempt from claims of creditors?

As a general rule, all companies established in Vietnam will be subject to the provisions of the Bankruptcy Law 2014. Unlike its predecessor, which provided for exceptions to insolvency proceedings (eg, special enterprises directly servicing national defence and security, companies operating in the sectors of finance, banking and insurance, and companies operating in sectors which regularly and directly provide essential public utility services (Special Companies)), the Bankruptcy Law 2014 does not provide for any exceptions other than the bankruptcy of credit institutions (see below).

Notwithstanding that the Bankruptcy Law 2014 does not contemplate different insolvency proceedings for Special Companies, since the regulations implementing the old bankruptcy law applicable to Special Companies have not been specifically repealed, the courts could still refer to such regulations when handling insolvency proceedings of such Special Companies. If so, the procedure would be slightly different (see question 4).

#### Special regimes applicable to credit institutions

The Bankruptcy Law 2014 provides for special insolvency proceedings in respect of credit institutions, which includes banks, finance companies and finance leasing companies. Under the Bankruptcy Law 2014, before the court accepts a bankruptcy petition (see step 2 referred to in question 26), an insolvent credit institution must have undergone the 'special control' imposed by the State Bank of Vietnam (the SBV) in accordance with relevant regulations of the SBV. The court will only accept the bankruptcy petition if the SBV has issued a written decision on termination of the 'special control' regime or cessation of application of special measures for recovery.

#### Excluded assets

If any credit institution that has received special loans from the SBV or from other credit institutions is declared bankrupt, it must return such special loans to the SBV or other credit institutions prior to distribution of assets to other creditors.

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## Public enterprises

### 4 What procedures are followed in the insolvency of a government-owned enterprise? What remedies do creditors of insolvent public enterprises have?

As noted in question 3, there is a possibility that the court would apply the regulations implementing the old bankruptcy law on Special Companies. Accordingly, upon receiving the bankruptcy petition in respect of a Special Company, the court is obliged to inform the state agency overseeing the Special Companies so that the relevant state agency can first apply 'recovery measures', and the court can only accept the bankruptcy petition if the state agency has issued a written decision on termination or cessation of the 'recovery measures'. Under the regulations, the list of Special Companies is to be promulgated by the relevant state agencies. However, to our knowledge, no such list has been promulgated.

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## Protection for large financial institutions

### 5 Has your country enacted legislation to deal with the financial difficulties of institutions that are considered 'too big to fail'?

No. However, in practice, the state has in the past 'propped up' institutions such as banks and shipping companies that it considers 'too big to fail'.

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## Secured lending and credit (immovables)

### 6 What principal types of security are taken on immovable (real) property?

Security over immovable (real) property should be created through a mortgage. A mortgage is an arrangement whereby the mortgagor uses

its assets, without handing over possession of the assets to the mortgagee, as security for the performance of an obligation.

### Secured lending and credit (moveables)

#### 7 What principal types of security are taken on moveable (personal) property?

Security over moveable (personal) property can be created through either a mortgage (see above) or pledge. A pledge is an arrangement whereby the pledgor hands over possession of an asset to the pledgee as security for the performance of an obligation.

### Unsecured credit

#### 8 What remedies are available to unsecured creditors? Are the processes difficult or time-consuming? Are pre-judgment attachments available? Do any special procedures apply to foreign creditors?

##### Remedies available to unsecured creditors

Under the Civil Code 2005 (National Assembly, 14 June 2005) a possessory lien is not considered to be a form of 'secured transaction'. The rights of a party with a possessory lien are as follows: 'the obligee ... who is legally possessing the property being the object of a bilateral contract is entitled to retain the property when the obligor fails to perform the obligations or has performed the obligations not strictly as agreed upon'.

However, from 1 January 2017 when the Civil Code 2015 (National Assembly, 24 November 2015) will take effect, a possessory lien will be considered to be a form of a 'secured transaction', so from that date a creditor possessing property under a lien would be considered to be a secured creditor for the purposes of the Bankruptcy Law 2014.

##### Right of unsecured creditors

The Bankruptcy Law 2014 makes a fundamental distinction between (i) fully secured creditors and (ii) unsecured creditors and partially secured creditors. A fully secured creditor is not entitled to file a bankruptcy petition nor vote in the creditors' meeting, while unsecured and partially secured creditors are entitled to do so (see question 26 for more detail).

##### Pre-judgment attachments

At the request of persons who have the right or obligation to make bankruptcy filing or the receiver (as defined in question 26), the court may issue a decision to apply an interim relief during insolvency proceedings, for example, permission for the sale of certain assets such as perishable goods, attachment and sealing up of assets of the company, freezing of bank accounts of the company, freezing assets and prohibiting the transfer of property.

##### Procedures applicable to foreign creditors

There are no special procedures applicable to foreign creditors.

### Voluntary liquidations

#### 9 What are the requirements for a debtor commencing a voluntary liquidation case and what are the effects?

There are two different procedures for the voluntary liquidation of a company: voluntary liquidation in accordance with the Enterprise Law and the charter (equivalent to the memorandum and articles of association) of the company; and voluntary liquidation in accordance with the Bankruptcy Law by filing a petition.

##### Voluntary liquidation under the Enterprise Law

A company established in Vietnam can be liquidated and dissolved in accordance with decision of its owners, members or shareholders. The requirements for passing a liquidation/dissolution decision are subject to the company's charter.

The winding up of a company will generally be carried out as follows:

- the owners, members or shareholders of the company pass a decision on liquidation and dissolution of the company;
- the company will notify the business registration body of the decision on liquidation and dissolution within seven business days of the issuance of the decision;

- the owners, members or the board of directors (as the case may be) of the company will be responsible for liquidating the company, or, if the company's charter so provides, a liquidation board will be established to carry out the liquidation of the assets of the company;
- after completion of liquidation and payment of all outstanding debts and liabilities, the company will prepare a report and submit the dissolution file to the business registration body; and
- the business registration body will deregister the company from the company registry (ie, the National Registration Portal) within five business days of the receipt of the complete dissolution file or 180 days of the receipt of the decision on liquidation and dissolution unless otherwise objected by relevant parties.

##### Voluntary liquidation under the Bankruptcy Law

If a company becomes insolvent, the company can be liquidated according to the steps discussed in question 26, and the company will be liquidated after the judge declares the company bankrupt (step 8).

### Involuntary liquidations

#### 10 What are the requirements for creditors placing a debtor into involuntary liquidation and what are the effects?

Creditors can only place a debtor into involuntary liquidation through insolvency proceedings.

### Voluntary reorganisations

#### 11 What are the requirements for a debtor commencing a formal financial reorganisation and what are the effects?

There are no regulations governing a financial reorganisation commenced by a debtor outside insolvency proceedings. Reorganisation is a matter of agreement between the debtor and its creditors. Depending on the nature of the arrangement, the reorganisation may be subject to provisions of:

- the Enterprise Law and its implementing regulations, which apply to corporate governance and operation of companies in Vietnam;
- the Investment Law (National Assembly, 29 November 2014) and its implementing regulations, which apply to the investment by investors in projects in Vietnam; and
- banking regulations which apply to financing activities in Vietnam.

### Involuntary reorganisations

#### 12 What are the requirements for creditors commencing an involuntary reorganisation and what are the effects?

As is the case for voluntary reorganisations, there are no regulations governing a financial reorganisation commenced by a creditor outside of insolvency proceedings.

### Mandatory commencement of insolvency proceedings

#### 13 Are companies required to commence insolvency proceedings in particular circumstances? If proceedings are not commenced, what liabilities can result? What are the consequences if a company carries on business while insolvent?

##### Obligations to commence insolvency proceedings

Under the Bankruptcy Law 2014, the following are obliged to make a bankruptcy filing if such person becomes aware that the company has become 'insolvent':

- the legal representative of the company, being the person identified in the enterprise registration certificate or the equivalent document as such (being either the chairman, chief executive officer or another person); and
- the owner of a single member limited liability company, the chairman of the members' council of a two or more member limited liability company, or the chairman of the board of directors of a joint stock company.

##### Liabilities for failure to commence insolvency proceedings

If a person specified above fails to make a bankruptcy filing upon becoming aware that the company has become 'insolvent', he or she would be subject to a monetary fine ranging from 1 million dong to 3 million dong (US\$50 to US\$100). In part because of the size of the

potential fine, very few companies have filed bankruptcy petitions notwithstanding the insolvency of a large number of companies.

### Doing business in reorganisations

#### 14 Under what conditions can the debtor carry on business during a reorganisation? What conditions apply to the use or sale of the assets of the business? Is any special treatment given to creditors who supply goods or services after the filing? What are the roles of the creditors and the court in supervising the debtor's business activities? What powers can directors and officers exercise after insolvency proceedings are commenced by, or against, their corporation?

There are two different procedures for the reorganisation of a company: reorganisation as part of insolvency proceedings and reorganisation pursuant to agreement between the debtor and creditors. In the latter case, the manner of conducting business in reorganisation will be subject to agreement between the parties.

In the absence of specific laws and regulations governing the reorganisation of a company (either voluntary or involuntary) and because reorganisation is generally a matter of agreement between the debtor and its creditors, for the purpose of this chapter, unless the contrary is stated, all reference to reorganisation will be to reorganisation as a part of insolvency proceedings.

#### Carrying on business during a reorganisation

In general, after the court issues the decision for commencement of insolvency proceedings (step 3), the company will continue to operate the business but will be subject to the supervision of the judge and the receiver. In particular:

- following the issuance of the decision to commence insolvency proceedings, and before issuance of the decision to recognise the resolutions of the creditors' meeting approving the recovery plan (step 6):
  - the company is prohibited from:
    - concealing, disposing of or donating any assets;
    - paying any unsecured debts except for the unsecured debts arising subsequent to the commencement of bankruptcy procedure and paying wages to employees of the company;
    - abandoning any right to claim a debt; and
    - converting unsecured debts into debts secured or partly secured by the assets of the company;
  - the company must report to, and obtain the consent of, the receiver prior to carrying out the following activities:
    - borrow or pledge, mortgage, guarantee, purchase, sale, assignment, leasing out of the assets; sale or conversion of the shares; transfer of the ownership rights in any asset;
    - termination of performance of an effective contract;
    - making payment for debts arising subsequent to the commencement of the insolvency proceedings; and
    - paying wages to employees; and
- following the issuance of the decision to recognise the resolution of the creditors' meeting approving the recovery plan (step 6):
  - business operations, including the use or sale of assets, of the company should be carried out in accordance with the approved recovery plan and under the supervision of the receiver and creditors; and
  - every six months, the company must report on the status of implementation of the recovery plan to the receiver who will then be responsible for reporting to the judge and creditors.

#### Treatment of creditors supplying goods or services after the filing

See the response to question 16.

#### Powers of directors and officers after the commencement of insolvency proceedings

After the commencement of insolvency proceedings, directors and officers still have the authority to manage business operations but subject to restrictions and the supervision of the judge and the receiver as discussed above. However, at the request of the creditors' meeting or the receiver, the judge may change the legal representative of the insolvent company.

### Stays of proceedings and moratoria

#### 15 What prohibitions against the continuation of legal proceedings or the enforcement of claims by creditors apply in liquidations and reorganisations? In what circumstances may creditors obtain relief from such prohibitions?

Under article 41 of the Bankruptcy Law 2014, within five business days of the date of the court's acceptance of the bankruptcy petition (step 2), the following proceedings and actions are temporarily suspended:

- enforcement a court/arbitral judgment, award or decision against assets of the company, except for enforcement of any judgment, award or decision obliging the insolvent company to compensate for life, health and honour or to pay wages to employees;
- civil, business, commercial or labour legal proceedings (but not criminal or administrative proceedings) to which the insolvent company is a party; and
- enforcement of security over assets of the insolvent company by secured creditors, except for assets that are exposed to a risk of being destroyed or a considerable decrease in value.

If the court decides to not issue a decision for commencement of insolvency proceedings (step 3), the stay discussed above will be lifted.

However, if the court decides to issue a decision for commencement of insolvency proceedings (step 3), the enforcement of a court judgment/arbitral award will be suspended. Such suspension will be lifted if the court decides to terminate the insolvency proceeding because the company is no longer 'insolvent' or the recovery plan terminates.

As regards the enforcement of security over assets, it will be subject to decision of the creditors' meeting if the collateral is needed for business recovery. Such enforcement may resume if the receiver recommends resuming the enforcement of the secured assets and when the bankrupt company is liquidated (step 8).

### Post-filing credit

#### 16 May a debtor in a liquidation or reorganisation obtain secured or unsecured loans or credit? What priority is given to such loans or credit?

As discussed in question 14, after the commencement of insolvency proceedings (step 3) the company still continues its business operations subject to the supervision of the judge and the receiver. Furthermore, after the court issues the decision for recognition of the resolution of the creditors' meeting approving the recovery plan (step 6), business operations of the company should be carried out in accordance with the approved recovery plan and under the supervision of the receiver and creditors. Accordingly, the debtor may incur secured or unsecured debts after the filing of the bankruptcy petition.

Debts arising subsequent to the commencement of the insolvency proceedings that are used for business recovery of the company will take priority over other unsecured debts (see question 33).

### Set-off and netting

#### 17 To what extent are creditors able to exercise rights of set-off or netting in a liquidation or in a reorganisation? Can creditors be deprived of the right of set-off either temporarily or permanently?

Article 63 of the Bankruptcy Law 2014 specifically allows a creditor of an insolvent company to agree with the company to offset obligations arising out of contracts entered into between the parties prior to the date of the court's decision commencing the insolvency proceeding (step 3) provided that the set-off must be approved by the receiver, who is then responsible to report to the judge on the set-off.

There are, however, specific provisions relating to insolvency that could limit the operation of a set-off in certain circumstances. For instance, a set-off in the event of insolvency could be regarded as 'making payment or setting off an obligations in favour of the creditor under a contract under which the obligations are not due or in an amount greater than the obligations of the insolvent company' under article 59 of the Bankruptcy Law 2014 and accordingly be held invalid by the court. See the discussion in question 39.

Another problem is that the Bankruptcy Law 2014 provides that after receiving the court's decision on bankruptcy declaration (step 7),

a bank holding its accounts cannot settle debts owed by that company without approval of the judge.

### Sale of assets

**18 In reorganisations and liquidations, what provisions apply to the sale of specific assets out of the ordinary course of business and to the sale of the entire business of the debtor? Does the purchaser acquire the assets 'free and clear' of claims or do some liabilities pass with the assets? In practice, does your system allow for 'stalking horse' bids in sale procedures and does your system permit credit bidding in sales?**

The sale of assets after the issuance of decision on commencement of an insolvency proceeding (step 3) is subject to the consent of the receiver, who is responsible for reporting to the judge (see discussions in the response to question 14).

After the court issues the decision for recognition of the resolution of the creditors' meeting approving the recovery plan (step 6), the sale of assets of the company must be carried out in accordance with the approved recovery plan and under the supervision of the receiver and creditors.

In respect of secured assets, under article 53 of the Bankruptcy Law 2014, the enforcement of secured assets (including the sale of the secured assets) will be subject to the decision of the judge upon recommendation of the receiver according to the following principles:

- if the secured assets are needed for the business recovery (step 6), the use of the secured assets will be subject to the resolutions of the creditors' meeting;
- if the secured assets are not needed for business recovery, then the enforcement will be subject to the provisions of the security agreement; and
- if the secured assets are subject to risk of destruction or considerable decrease in value, the receiver may recommend the judge to permit the immediate enforcement of the assets.

When liquidating the assets under step 8 referred to in the response to question 26, the assets of the bankrupt company can be sold at auction or by private sale provided that moveable assets having a value of 10 million dong and above, and real property must be sold by auction.

The ownership of a purchaser acquiring assets from an insolvent company in a manner not in accordance with the above requirements is open to question. Indeed, given that Vietnamese law is so general and ambiguous, there is no guarantee that a purchaser's ownership is 'free and clear' of claims even where a purchaser acquires assets in accordance with the above requirements.

### 'Stalking horse' bids and credit bidding

The regulations on action sale do not contemplate the use of 'stalking horse' bids or credit bidding.

### Intellectual property assets in insolvencies

**19 May an IP licensor or owner terminate the debtor's right to use it when an insolvency case is opened? To what extent may an insolvency administrator continue to use IP rights granted under an agreement with the debtor? May an insolvency representative terminate a debtor's agreement with a licensor or owner and continue to use the IP for the benefit of the estate?**

There is no automatic right of a licensor or owner of IP to terminate the debtor's right to use IP assets. Such matters will be governed by the terms of the licence, for example, in the event of default and termination provisions. As discussed in question 21, the court may decide to temporarily suspend and/or terminate a debtor's contract.

### Personal data in insolvencies

**20 Where personal information or customer data collected by an insolvent company is valuable to its reorganisation, are there any restrictions in your country on the use of that information in the insolvency or its transfer to a purchaser?**

The Bankruptcy Law 2014 does not provide for specific requirements for the use of personal information or customer data collected by an

insolvent company during the insolvency proceedings. This is subject to the agreement between the insolvent company and the persons providing information and data and regulations on the collection, storage and use of personal information or customer data including the Civil Code and the Law on Information Technology.

### Rejection and disclaimer of contracts in reorganisations

**21 Can a debtor undergoing a reorganisation reject or disclaim an unfavourable contract? Are there contracts that may not be rejected? What procedure is followed to reject a contract and what is the effect of rejection on the other party? What happens if a debtor breaches the contract after the insolvency case is opened?**

Article 61 of the Bankruptcy Law 2014 allows a creditor or the debtor to request that the court temporarily suspends the implementation of a contract that could have an adverse effect on the debtor. The law suggests that such request must be made within five business days of the date of the acceptance of the bankruptcy petition (step 2).

In addition, within five business days from the date when the people's court issues the decision to commence the insolvency proceeding (step 3), the court must review the temporarily suspended contracts and decide whether to:

- continue the performance of the contract if the performance will not cause any disadvantage to the company; or
- terminate the contract, in which case the counterparty may be awarded damages and it will have the same rights as an unsecured creditor in respect of such damages.

### Arbitration processes in insolvency cases

**22 How frequently is arbitration used in insolvency proceedings? Are there certain types of insolvency disputes that may not be arbitrated? Will the court allow arbitration proceedings to continue after an insolvency case is opened? Can disputes that arise in an insolvency case after the case is opened be arbitrated with the consent of the parties? Can the court direct the parties to such disputes to submit them to arbitration?**

Following the court's acceptance of the bankruptcy petition (step 2 referred to in question 26), the legal proceedings, including arbitration proceedings must be temporarily or permanently suspended (see question 15). The Bankruptcy Law 2014 is silent on arbitration proceedings arising post-filing, and it is not clear how the court will handle such arbitration proceedings.

### Successful reorganisations

**23 What features are mandatory in a reorganisation plan? How are creditors classified for purposes of a plan and how is the plan approved? Can a reorganisation plan release non-debtor parties from liability, and, if so, in what circumstances?**

#### Recovery plan

After the commencement of insolvency proceedings and before the entry into a bankruptcy decision, the insolvent company may be required to formulate the recovery plan. See step 6 discussed in question 26.

The recovery plan must be approved by the creditors' meeting.

Once the recovery plan is completed as planned, the judge will decide to terminate the 'operation recovery' process and the company is no longer deemed to be insolvent.

#### Release of non-debtor parties from liability

As discussed in question 21, the court may temporarily suspend and then terminate the implementation of a contract that could have an adverse effect on the debtor. Accordingly, a non-debtor party may be released from liability under such contracts.

### Expedited reorganisations

**24 Do procedures exist for expedited reorganisations?**

Although there are expedited procedures for the court to issue a bankruptcy decision (step 7), there are no such procedures for expedited reorganisations. The implementation time will depend on the complexity and the approval by the creditors.

## Unsuccessful reorganisations

### 25 How is a proposed reorganisation defeated and what is the effect of a reorganisation plan not being approved? What if the debtor fails to perform a plan?

As discussed in the response to question 23, a creditors' meeting should take place to decide if the insolvent company should propose a recovery plan. If the creditors' meeting decides to propose that the court declares the bankruptcy, then within 15 days of receipt of a report on results of the creditors' meeting, the judge should issue a decision declaring that the company is bankrupt.

If the creditors' meeting decides that the insolvent company should propose a recovery plan, then the insolvent company should propose a recovery plan in accordance with procedures discussed in the response to question 23. However, if the insolvent company fails to propose a recovery plan within the time limit or the creditors' meeting does not approve the proposed recovery plan, the judge should issue a decision declaring the company bankrupt.

If the creditors' meeting approves a recovery plan, but the insolvent company fails to implement the recovery plan, the judge should issue a decision declaring the company bankrupt.

## Insolvency processes

### 26 During an insolvency case, what notices are given to creditors? What meetings are held? How are meetings called? What information regarding the administration of the estate, its assets and the claims against it is available to creditors or creditors' committees? What are insolvency administrators' reporting obligations? May creditors pursue the estate's remedies against third parties?

#### Insolvency process

The bankruptcy process under the Bankruptcy Law 2014 is as follows:

#### Step 1: Filing bankruptcy petition

Court-driven insolvency proceedings may be commenced by, among others, an unsecured creditor or partially secured creditor, the legal representative or the owner of the insolvent company, or a union representative or elected representative of employees.

#### Step 2: Court's acceptance of the bankruptcy petition

After the acceptance of the bankruptcy petition: within three business days after receipt, the court should notify the acceptance to the petitioner in writing or, if it is the insolvent company which files the bankruptcy petition, all creditors of the company as provided by the company. The insolvent company and the creditor filing such petition may request that the court postpones the acceptance in order for the parties to negotiate the withdrawal of the petition.

#### Step 3: Court's decision on commencement of an insolvency proceeding

It is possible that the court could decide to reject the petition if it believes that it would be inappropriate to continue with the bankruptcy proceeding. After the issue of a decision to commence insolvency proceedings, the court should send the decision to, among others:

- the person filing the petition;
- the insolvent company; and
- creditors, and must post the decision on the National Registration Portal (ie, the company registry) and publish it in two consecutive editions of local newspapers.

#### Step 4: Appointees and duties

The appointment of an asset management officer or a firm in charge asset management and liquidation (in this chapter, referred to as the receiver), preparation of the asset inventory, the list of creditors and the list of debtors.

This receiver is appointed by the court. It is possible for the person filing the petition to propose a receiver to the court, and the judge can appoint such person if they have sufficient qualifications and there is no conflict of interest. The identity of the receiver will be published together with the decision to call a creditors' meeting. The receiver plays a role similar to that of a receiver (or in case of liquidation, liquidator) in bankruptcy proceedings.

The insolvent company must conduct a full inventory of assets within 30 days of the date of the decision to commence insolvency proceedings which may be extended twice, each time for not more than 30 days.

Within 30 days of the date of the decision to commence insolvency proceedings, creditors must send their claims to the receiver, and the list of creditors will be established within 15 days thereafter. The list of creditors of the insolvent company must be publicly posted at the head office of the court, the registered head office of the insolvent company and the National Registration Portal and sent to creditors who made claims within 10 business days of the date of posting. A creditor or the insolvent company may request the judge to adjust the list of creditors.

The list of debtors of the insolvent company must be prepared and publicly posted at the head office of the court and the registered head office of the insolvent company within 45 days of the date of the decision to commence the insolvency proceedings and sent to creditors who made claims within 10 business days of the date of posting.

#### Step 5: Holding creditors' meetings

The creditors' meeting provides a forum for the receiver to report to the creditors on the financial situation of the insolvent company, the results of asset inventories and debtor and creditor lists, for the insolvent company's management to express their views on the reports of the receiver and to propose a restructuring plan, as well as for the creditors and interested parties to express their views on specific matters to be resolved.

The creditors' meeting has the authority to:

- request the suspension of the insolvency proceedings if the debtor has not become insolvent;
- request to proceed with business restoration;
- request for bankruptcy;
- approve a recovery plan; and
- appoint the members of a representative board of creditors (see discussions at question 28).

All creditors named on the list of creditors have the right to attend the meeting. A creditor may appoint a proxy to attend the meeting on its behalf.

To convene a creditors' meeting, the judge must send a notice of the creditors' meeting and other relevant documents to creditors no later than 15 days prior to the meeting. The notice and accompanying documents must be delivered by hand or sent by registered or non-registered mail, fax, telex or email or by other means provided that the sending is recorded. The notice must specify the time, venue, agenda and contents of the creditors' meeting.

A quorum of creditors' representing at least 51 per cent of the total value of unsecured debt must be present, and a resolution of the creditors' meeting is carried when approved by a simple majority of those unsecured creditors in attendance representing at least 65 per cent of the total unsecured debt amount.

#### Step 6: Rehabilitation of the business

In the event that the creditors' meeting passes a resolution to the effect that recovery measures should be applied, there is a 30-day window for the insolvent company to formulate a detailed plan for recovery (the recovery plan) which should include, inter alia, at least certain of the following measures: raising capital, changing business lines, disposing of unnecessary assets, selling shares to creditors and restructuring management. The recovery plan must be first sent to the judge, the creditors and the receiver for comments and then approved by the creditors' meeting.

After the recovery plan is approved by the creditors' meeting, the implementation of the recovery plan will be under supervision of the receiver and creditors. As discussed in the response to question 28, a representative board of creditors may, acting on behalf of the creditors, be appointed to supervise the implementation of the resolutions of the creditors' meeting and request the receiver to implement the resolutions of the meeting of creditors. During the process of implementation of the recovery plan, once every six months, the insolvent company must report on the status of implementation the plan to the receiver who shall be responsible for reporting to the judge and notifying creditors.

The time-limit for implementation of the recovery plan will be decided by the creditors' meeting. If the creditors' meeting fails to

specify a time-limit, the time-limit for implementation of such plan will not exceed three years from the date it is approved by the creditors' meeting.

#### **Step 7: Declaration of bankruptcy**

The judge will declare the company bankrupt and insolvency proceedings would move into the liquidation phase if:

- the creditors' meeting could not be convened;
- the creditors' meeting could not pass any resolution;
- the creditors' meeting did not approve or could not pass the resolution on the recovery plan;
- the creditors' meeting requested for declaring the company bankrupt; or
- the insolvent company could not formulate the recovery plan within the time limit or failed to implement the recovery plan.

Within 10 business days of issuing the bankruptcy decision, the court must send the decision to, among others, the person filing the petition, the insolvent company and creditors, and must post the decision on the National Registration Portal (ie, the companies registry) and publish it in two consecutive editions of a local newspaper.

#### **Step 8: Liquidation of assets**

Assets of the bankrupt company can be sold by auction or private sale (see the response to question 18). After the liquidation and distribution of the assets is completed, the judgment enforcement agency will decide to terminate the bankruptcy decision.

#### **Claim against third parties**

Vietnamese bankruptcy law does not provide any grounds for a creditor to bring proceedings against third parties in relation to losses suffered by the company.

#### **Enforcement of estate's rights**

##### **27 If the insolvency administrator has no assets to pursue a claim, may the creditors pursue the estate's remedies? If so, to whom do the fruits of the remedies belong?**

While the insolvent company may incur additional debts after the bankruptcy filing (see question 16), which could arguably be used for pursuing a claim, the bankruptcy law does not provide for circumstances that the creditors pursue a claim by themselves. Any fruits of the remedies will belong to the insolvency estate and distributed in the manner discussed in the response to question 33.

#### **Creditor representation**

##### **28 What committees can be formed (or representative counsel appointed) and what powers or responsibilities do they have? How are they selected and appointed? May they retain advisers and how are their expenses funded?**

The creditors' meeting may appoint a representative board of creditors, composed of between three and five members. The representative board of creditors will, acting on behalf of the creditors, supervise the implementation of the resolutions of the creditors' meeting and request the receiver to implement the resolutions of the meeting of creditors. If the receiver fails to carry out such request, the representative board of creditors may report such failure in writing to the judge. The Bankruptcy Law 2014 gives no guidance as to how to appoint members of a representative board of creditors.

The Vietnamese bankruptcy law is silent on whether the representative board of creditors may retain advisers and, if so, how their expenses would be funded.

#### **Insolvency of corporate groups**

##### **29 In insolvency proceedings involving a corporate group, are the proceedings by the parent and its subsidiaries combined for administrative purposes? May the assets and liabilities of the companies be pooled for distribution purposes? May assets be transferred from an administration in your country to an administration in another country?**

Under Vietnamese law, each member of a corporate group is a separate legal entity except in very specific circumstances. Accordingly, the

assets and liabilities of companies are not combined into one pool for distribution in an insolvency process.

There is no legal basis for the transfer of assets subject to administration under insolvency in Vietnam to an administration in another country.

#### **Appeals**

##### **30 What are the rights of appeal from court orders made in an insolvency proceeding? Does an appellant have an automatic right of appeal or must it obtain permission to appeal? Is there a requirement to post security to proceed with an appeal and, if so, how is the amount determined?**

##### **Rights to appeal court orders made in an insolvency proceeding**

Under Vietnamese bankruptcy law, certain decisions of the court made in an insolvency proceeding can be appealed. In particular:

- if, after receipt of the bankruptcy petition (step 1), the court decides to object to the petition, within three business days from the date of receipt an objection decision, the petitioner or the people's procuracy at the same level may appeal the decision by requesting the chief judge of the court which made the decision to reconsider. If the petitioner or the people's procuracy is not satisfied with the decision of the chief judge on reconsideration, a further appeal may be made to the chief judge of the court at an immediately higher level, whose decision will be final;
- after the acceptance of the bankruptcy petition (step 2), the court may decide whether or not to commence insolvency proceedings. The decision can be appealed by any participant in the insolvency proceedings (ie, creditors, debtors, employees, the insolvent company and its shareholders and other relevant persons) or the people's procuracy at the same level. The request must be sent within seven business days of the date of receiving the decision to commence or not to commence insolvency proceedings. The immediately higher court has the authority to consider the appeal request, and that decision will be final;
- after the court issues a decision to declare the company bankrupt (step 7), the petitioner, the insolvent company, creditors, or the people's procuracy may appeal the decision within 15 days of the date of receiving the decision. The immediately higher court has the authority to consider the appeal request. The decision of the higher court may be further reconsidered by the Supreme Court at the request of a participant in the insolvency proceedings or the Supreme People's Procuracy;
- during insolvency proceedings, the court may issue a decision to declare a transaction invalid (see questions 39 and 40). Within five business days of the date of receiving a decision declaring a transaction invalid, the insolvent company or the counterparty to the transaction may make a written request to the chief judge of the court which made the decision to reconsider the decision, whose decision will be final; and
- during insolvency proceedings, the court may issue a decision to apply interim relief (see question 8 – pre-adjustment attachments). Any participant in the insolvency proceedings or the people's procuracy at the same level may appeal the decision to the chief judge of the court that made the decision, whose decision will be final.

##### **Requirement to post security to proceed with an appeal**

There is no requirement to post security to proceed with an appeal.

#### **Claims**

##### **31 How is a creditor's claim submitted and what are the time limits? How are claims disallowed and how does a creditor appeal? Are there provisions on the transfer of claims? Must transfers be disclosed and are there any restrictions on transferred claims? Can claims for contingent or unliquidated amounts be recognised? How are the amounts of such claims determined?**

##### **Submission of creditor's claims**

Except in the event of force majeure, within 30 days of the date of the decision to commence an insolvency proceeding (step 3), creditors must send the claim for debts to the receiver.

The claim must be accompanied by supporting documents, and be signed by the creditor or his or her legal representative.

#### List of creditors and appeal

The list of creditors will be prepared by the receiver within 15 days after the deadline for submission of claims. The list of creditors must be publicly posted at the head office of the court, the registered head office of the insolvent company and the National Registration Portal and sent to creditors who made claims within 10 business days from the date of posting.

A creditor or the insolvent company may request the judge to adjust the list of creditors within five business days after the ending date of posting. However, the bankruptcy law is silent on how long the list of creditors will be posted and what will be the ending date of posting.

#### Transfer of claims

Vietnamese bankruptcy law does not contemplate the purchase, sale or transfer of claims. Since the Bankruptcy Law 2014 does not provide procedures for changing the list of creditors once it has been prepared, it is not clear if the court would accept the transferee of a claim to be a new creditor, entitled to rights as a creditor of the insolvent company in the insolvency proceedings.

#### Amounts of claims and interests

The amount of claims against the insolvent company created before the date of commencement of insolvency proceedings will be determined at the time of issuing the decision to commence the insolvency proceeding (step 3).

The amount of claims against the insolvent company created after the court's decision to commence the bankruptcy procedure will be determined at the time of issuing the decision to declare bankruptcy (step 7).

After the decision to commence the insolvency proceeding (step 3), interest is still accrued on outstanding loans but the payment of the interest will be temporarily suspended. After the decision to declare bankruptcy (step 7), no interest will be accrued on loans. As for new debts obtained after the commencement of the insolvency proceedings, the interest on such debts will be determined as agreed between the lender and the debtor.

#### Modifying creditors' rights

##### 32 May the court change the rank of a creditor's claim? If so, what are the grounds for doing so and how frequently does this occur?

The court does not have general jurisdiction to change the priority of creditors' claims, which are determined by statute.

#### Priority claims

##### 33 Apart from employee-related claims, what are the major privileged and priority claims in liquidations and reorganisations? Which have priority over secured creditors?

The liquidated assets of the bankrupt company (excluding those assets being subject to valid security interest) are distributed in the following order (step 8):

- first, costs and expenses related to the bankruptcy proceeding;
- second, unpaid wages, severance allowances, social insurance and health insurance and other employee benefits;
- third, debts arising subsequent to the commencement of the insolvency procedure that are used for the purpose of business recovery of the company;
- fourth, financial obligations to the state; unsecured debts payable to the creditors named in the list of creditors; and secured debts that remain unpaid because of the value of the secured assets being insufficient to repay them; and
- the remaining assets will be distributed to the owner or owners of the bankrupt company.

#### Distribution of liquidated assets of bankrupt credit institutions

Unlike other normal companies, the assets of a bankrupt credit institution are distributed differently. The insolvent credit institution receiving special loans from the SBV or from other credit institutions is

required to return such special loans to the SBV or other credit institutions in priority to the distribution of assets to other creditors.

After the payment of special loans, the liquidated assets of the bankrupt credit institution are distributed in the following order:

- first, costs and expenses related to the bankruptcy proceeding;
- second, unpaid wages, severance allowances, social insurance and health insurance and other employee benefits;
- third, deposits; amounts payable by deposit insurance institutions to depositors;
- fourth, financial obligations to the state; unsecured debts payable to the creditors named in the list of creditors; and secured debts that remain unpaid because of the value of the secured assets being insufficient to repay them; and
- the remaining assets will be distributed to the owner or owners of the bankrupt credit institution.

#### Employment-related liabilities in restructurings

##### 34 What employee claims arise where employees are terminated during a restructuring or liquidation? What are the procedures for termination?

Employment contracts can be unilaterally terminated by the company in the case of restructuring of the company or liquidation of the company, as a part of the insolvency proceedings or otherwise.

#### Termination because of restructuring

Under article 44 of the Labour Code of Vietnam (National Assembly, 18 June 2012), an employer may unilaterally terminate the employment with its employee because of 'organisational restructuring' or 'economic reasons'.

In the event that the employment is terminated pursuant to article 44 of the Labour Code, the termination must be carried in accordance with the following procedures:

- first, the employer must prepare a restructuring plan (the employment restructuring plan), which includes, among others, information on the concerned employees whose labour contracts will be terminated;
- if the employment restructuring plan results in termination of employment with multiple employees, the trade union of the company must be consulted on the plan; and thereafter notified to the labour authority. The law only requires the company to consult with the trade union and to notify the plan to the labour authority, but it does not require any consent of the trade union or the labour authority; and
- the employment can only be terminated after the date falling 30 days after the date of notification to the labour authority.

At law, if the termination of employment is because of restructuring under article 44 of the Labour Code, employees are entitled to a redundancy allowance equal to the aggregate amount of one month's salary and benefits for every year of service, subject to a minimum payment of two months' salary and benefits. However, if the employer has paid unemployment insurance for the terminated employees for the period after 1 January 2009, the redundancy allowance will only be paid in respect of the working period prior to 1 January 2009. For the working period after 1 January 2009, the employees are entitled to an unemployment allowance to be paid by the state. In addition to the redundancy allowance, upon termination of an employment contract, the employer would also be required to make other payments, including:

- payment of salary in lieu of any accrued annual leave that has not been taken by the employee prior to the termination; and
- any other amounts payable under existing labour contracts and collective labour agreement (if any).

#### Termination because of liquidation

Under the Labour Code, once a company is liquidated, the employment contracts between the company and its employees are terminated.

Unlike the termination because of restructuring as discussed above, if the employment is terminated because of liquidation of the employer, the employees are entitled to a severance allowance, which is equal to the aggregate amount of half of one month's salary for each year of employment but, like the redundancy allowance, the company is not required to pay severance allowance for the period that it has

paid unemployment insurance, which may have been effected since 1 January 2009. In addition to the severance allowance, upon the termination of a labour contract, the employer would also be required to make other payments, including:

- payment of salary in lieu of any accrued annual leave that has not been taken by the employee prior to the termination; and
- any other amounts payable under the existing labour contracts and collective labour agreement (if any).

#### **Pension claims**

#### **35 What remedies exist for pension-related claims against employers in insolvency proceedings and what priorities attach to such claims?**

In the case of liquidation of a bankrupt company, claims of employees will rank behind claims for costs and expenses related to the bankruptcy proceedings (and claims of secured creditors in respect of the secured assets) – see the answer to question 33.

#### **Environmental problems and liabilities**

#### **36 In insolvency proceedings where there are environmental problems, who is responsible for controlling the environmental problem and for remediating the damage caused? Are any of these liabilities imposed on the insolvency administrator, secured or unsecured creditors, the debtor's officers and directors, or on third parties?**

Environmental damage could give rise to civil liabilities, administrative liabilities and criminal liabilities.

In general, the legal representative of the company causing environmental problem is responsible for the consequences, including criminal liability if such violation amounts to criminal liability, and the company causing environmental problem is responsible for damages, if any. The insolvency administrator, secured or unsecured creditors are generally not responsible for environment problems caused by the debtor.

#### **Liabilities that survive insolvency proceedings**

#### **37 Do any liabilities of a debtor survive an insolvency or a reorganisation?**

If the debtor is liquidated after being declared bankrupt, there are no surviving liabilities.

#### **Distributions**

#### **38 How and when are distributions made to creditors in liquidations and reorganisations?**

See question 33.

#### **Transactions that may be annulled**

#### **39 What transactions can be annulled or set aside in liquidations and reorganisations and what are the grounds? What is the result of a transaction being annulled?**

Under article 59 of the Bankruptcy Law 2014, the following transactions may be held by the court to be invalid if conducted within six months prior to the date of commencement of an insolvency proceeding (step 3):

- transfer of property that is not at market price;
- conversion of an unsecured debt into a secured debt or partly secured debt on the assets of the company;
- making payments, or setting off an obligations in favour of a creditor, where the debt is not yet due or in relation to a sum that is larger than the debt becoming due;
- donation of assets;
- conducting transactions outside the purpose of the business operations of the insolvent company; and
- other transactions for the purpose of 'dispensing' assets.

The six-month voidable period referred to above is extended to 18 months where the transaction is between the insolvent company and a 'related person'. The 'related persons' of an insolvent company are defined to include:

- (i) the parent company of the insolvent company, a manager of the parent company or any person who has the power to appoint such managers;
- (ii) any subsidiary company of the insolvent company;
- (iii) persons or a group of persons capable of controlling the decision making and operations of the insolvent company via its management bodies;
- (iv) a manager of the insolvent company;
- (v) the spouse, parent or foster parent, child, adopted child, or sibling of a manager of the insolvent company, or of a member or shareholder who holds the controlling capital contribution or shares in the insolvent company;
- (vi) any individual authorised to represent those identified in (i), (ii), (iii), (iv) and (v) above;
- (vii) any company in which any of the persons identified in (i), (ii), (iii), (iv), (v), (vi) above and (viii) below hold interests to the extent that they control the decision-making process of the management bodies of the company; and
- (viii) any group of persons who agree to act in concert in order to take over an interest in the insolvent company or in order to control the insolvent company.

If a transaction is declared to be invalid, any recovered assets must be included in the total assets of the insolvent company.

#### **Proceedings to annul transactions**

#### **40 Does your country use the concept of a 'suspect period' in determining whether to annul a transaction by an insolvent debtor? May voidable transactions be attacked by creditors or only by a liquidator or trustee? May they be attacked in a reorganisation or a suspension of payments or only in a liquidation?**

As discussed in the response to question 39, certain transactions may be declared invalid if they are entered into within six months or, in the case of transactions with related persons, 18 months prior to the date of commencement of an insolvency proceeding (step 3 referred to in question 26).

Any participants in insolvency proceedings (including creditors, debtors, employees, the insolvent company and its shareholders and other relevant persons) or the receiver may request the court to declare the relevant contract or transaction invalid. The court itself can declare a contract or transaction invalid if it is aware that the contract or transaction falls into circumstances provided for under article 59 of the Bankruptcy Law 2014.

#### **Directors and officers**

#### **41 Are corporate officers and directors liable for their corporation's obligations? Are they liable for pre-bankruptcy actions by their companies? Can they be subject to sanctions for other reasons?**

Officers and directors will not generally be personally liable for obligations of the company. However, officers can be held personally liable in the following circumstances:

- under both the Civil Code 2005 and the Civil Code 2015, a corporate officer and director of a company would be personally responsible for a transaction entered into by him or her without or beyond the scope of authorisation from the company unless the company consents to such transaction or is aware but has not objected to the transaction, or the other counterparty is aware of the lack of authorisation but agrees to proceed with the transaction;
- officers and directors of a company are generally responsible for executing their tasks honestly, and in a manner that they believe to be in the best interests of the company and with a degree of prudence; they are also required to avoid conflicts of interest. Officers and directors may be found liable in the event of breach of such duties; and
- the legal representative of a company may be held liable for directing the company to violate the law (eg, as discussed in the response to question 36). Under the current criminal law, criminal sanctions can only be applied to individuals, not to organisations – though under the new criminal law to be approved by the National Assembly criminal liability extends to bodies corporate.

As discussed in the response to question 13, certain officers of a company are obliged to make a bankruptcy filing if such person becomes aware that the company has become 'insolvent'.

Vietnamese law does not have the concept of a 'zone of insolvency' whereby months prior to an entity actually becoming insolvent, a higher degree of care is owed by executive officers and directors to the company and its creditors.

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### Groups of companies

#### 42 In which circumstances can a parent or affiliated corporation be responsible for the liabilities of subsidiaries or affiliates?

In principle, each corporate entity has its own existence and the corporate veil will only be rarely pierced, so the circumstances where a parent or affiliated company could be liable for its subsidiaries or affiliates are limited. However, the Enterprise Law contains certain specific exceptions to the limited liability principle, for example:

- if an owner or shareholder of a company fails to contribute the charter capital as committed, the owner or shareholder must be responsible for the company's liabilities to the extent of its committed capital;
- the owners or shareholder of a company is only permitted to withdraw capital from the company in the form of selling its interest in the company; in the case of withdrawal of all or part of its contributed charter capital from the company in another form, the owner or shareholder and the concerned person must be jointly liable for debts and other liabilities of the company;
- the owners or ordinary shareholders of a company are not permitted to be distributed profits if the company is unable to repay due debts; in the case of breaching this provision, the owner or shareholders must return the distributed profit; and
- transactions or contracts between a company (as one party) and its owners or shareholders and their related persons (as the other party) are considered to be related party transactions and must be approved by the relevant corporate bodies of the company.

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### Insider claims

#### 43 Are there any restrictions on claims by insiders or non-arm's length creditors against their corporations in insolvency proceedings taken by those corporations?

As discussed in the response to question 38, shareholders are last in the order of distribution in respect of their share capital, after the claims of unsecured creditors have been satisfied in full. Non-arm's length creditors will rank *pari passu* with the remainder of the unsecured creditors unless they have security (in which case they will rank in accordance with the security ranking) or their claims are related to debts arising subsequent to the commencement of the insolvency procedure that serves the purpose of business recovery of the company.

The suspect period for voidable transactions is extended from six months to 18 months in the case of transactions with related persons. See question 37 for more detail.

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### Creditors' enforcement

#### 44 Are there processes by which some or all of the assets of a business may be seized outside of court proceedings? How are these processes carried out?

A secured creditor can potentially enforce its security outside of court proceedings. Possessing the secured asset is one enforcement measure if it is agreed by the parties.

Before enforcing the security, the person foreclosing on the secured asset (realisor) must either deliver an enforcement notice to other secured parties or register the enforcement notice with the security registrar.

Secured assets may be foreclosed upon within a time limit agreed by the parties; or, if there is no such agreement, the realisor will have the right to make a decision on the time for realisation, which must not be earlier than seven days in the case of moveables and 14 days in the case of immovables, calculated from the date of the enforcement notice.

While the law technically permits secured creditors to foreclose on secured assets without the need for judicial proceedings or the permission of a court or any other party in Vietnam upon the occurrence of an event of default, in practice, the ease of enforcement depends upon numerous factors: the type of collateral, the cooperation of the securing party and the assistance of the authorities. In many instances, secured creditors are unable to enforce security without a court judgment and the subsequent assistance of the judgment enforcement team, which assists the secured party in enforcement of the judgment.

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### Corporate procedures

#### 45 Are there corporate procedures for the liquidation or dissolution of a corporation? How do such processes contrast with bankruptcy proceedings?

See question 9.

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### Conclusion of case

#### 46 How are liquidation and reorganisation cases formally concluded?

In the case of voluntary liquidation under the Enterprise Law, the liquidation of a company is completed once the business registration body deregisters the company from the company registry (ie, the National Registration Portal). See question 9 for more detail.

In the case of liquidation under the Bankruptcy Law 2014, the liquidation of a company is completed after completion of the distribution of assets, as discussed in the response to question 38, or after the judge declares the company bankrupt if the company has no assets to be liquidated and distributed.

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### International cases

#### 47 What recognition or relief is available concerning an insolvency proceeding in another country? How are foreign creditors dealt with in liquidations and reorganisations? Are foreign judgments or orders recognised and in what circumstances? Is your country a signatory to a treaty on international insolvency or on the recognition of foreign judgments? Has the UNCITRAL Model Law on Cross-Border Insolvency been adopted or is it under consideration in your country?

##### Recognition and assistance for foreign insolvency proceedings

Unless there is a treaty on legal assistance between Vietnam and the foreign country, the recognition and assistance of foreign insolvency proceedings in Vietnam is generally regulated by the Civil Procedure Code (National Assembly, 25 November 2015) and the Legal Assistance Law (National Assembly, 21 November 2007). Vietnam has only signed bilateral treaties on legal assistance with a few countries and territories, other than France and Republic of China (Taiwan), most of those countries were, or still are, communist states: Russia, Cuba, the Czech Republic, Slovakia, Hungary, Bulgaria, Poland, China, Laos and North Korea. Nor is Vietnam a signatory to any multilateral international conventions on reciprocal enforcement of judgments. Therefore the orders, decisions and judgments of most of the courts of developed jurisdictions would not be recognised in Vietnam.

Under the Legal Assistance Law, the relevant foreign body seeking a judicial assistance in Vietnam should send a civil legal mandate dossier to the Ministry of Justice of Vietnam requesting assistance. After examining the validity of the dossier, the Ministry of Justice of Vietnam will transfer it to the competent Vietnamese authority for implementation.

##### Foreign creditors

Foreign creditors will be able to provide evidence of their claims in Vietnamese liquidation proceedings in the normal way.

##### Enforcement of foreign court judgments

For the reason discussed above, judgments of foreign courts are generally unenforceable against assets in Vietnam.

**COMI**

**48** What test is used in your jurisdiction to determine the COMI (centre of main interests) of a debtor company or group of companies? Is there a test for, or any experience with, determining the COMI of a corporate group of companies in your jurisdiction?

Vietnamese insolvency law does not provide for the concept of the COMI (centre of main interests) of a debtor company or group of companies. Most foreign businesses establish a separate legal entity in Vietnam, and the insolvency proceedings of other members of the group are separate from those applied to the company in Vietnam.

**Cross-border cooperation**

**49** Does your country's system provide for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings? Have courts in your country refused to recognise foreign proceedings or to cooperate with foreign courts and, if so, on what grounds?

See question 47.

**Cross-border insolvency protocols and joint court hearings**

**50** In cross-border cases, have the courts in your country entered into cross-border insolvency protocols or other arrangements to coordinate proceedings with courts in other countries? Have courts in your country communicated or held joint hearings with courts in other countries in cross-border cases? If so, with which other countries?

No.



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# Quick reference tables

These tables are for quick reference only. They are not intended to provide exhaustive procedural guidelines, nor to be treated as a substitute for specific advice.

The information in each table has been supplied by the authors of the relevant chapter.

<b>AUSTRALIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Corporations Act 2001 (Cth).
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage (both equitable and legal).
	<b>Customary kinds of security devices on moveables</b>
	Security interest (charge, pledge, lien, etc) registered on the Personal Properties Securities Register.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	A moratorium on legal actions exists in both voluntary administration and liquidation. No such moratorium exists upon the commencement of a receivership.
	<b>Duties of the insolvency administrator</b>
	Insolvency practitioners have a number of duties including: <ul style="list-style-type: none"> <li>• to act with reasonable care and skill;</li> <li>• to act in good faith;</li> <li>• to act bona fide; and</li> <li>• to be independent.</li> </ul> Each insolvency administrator is also considered an officer of the company so must also comply with the duties of officers of the company (both statutory and at common law). Liquidators and administrators also considered fiduciaries and are held to a higher standard than receivers.
	<b>Set-off and post-filing credit</b>
	Available under section 553 of the Act. Operates automatically when there is a mutuality of transactions between the debtor and the creditor. Not available if the creditor knew of the debtor's insolvency.
	<b>Creditor claims and appeals</b>
	Proof of debts are filed in liquidation, administrations and schemes of arrangement. A similar process exists for all three. The insolvency practitioner maintains a high degree of discretion with respect to admitting (or rejecting) claims, and may require further information. Aggrieved creditors can seek recourse through the courts if a proof of debt is rejected. The courts have exhibited a reluctance to overturn decisions of independent insolvency practitioners.
	<b>Priority claims</b>
	Secured creditors have priority. Under section 556 of the Act certain other creditors are afforded a level of priority (including employees, providers of funding and the costs of the insolvency administrator).
	<b>Major kinds of voidable transactions</b>
	<ul style="list-style-type: none"> <li>• Uncommercial transactions;</li> <li>• unfair preferences;</li> <li>• unreasonable director-related transactions; and</li> <li>• unfair loans.</li> </ul>
	<b>Operating and financing during reorganisations</b>
	Financing permitted under all forms of Australian administration (voluntary administration, liquidation and receivership). Such financing is afforded a level of priority either under statute or existing security documents.
<b>International cooperation and communication</b>	
Australia has adopted the UNCITRAL Model Law on Cross-Border Insolvency by implementing legislation called the Cross-Border Insolvency Act 2008 (Cth).	
<b>Liabilities of directors and officers</b>	
Directors and offices may be liable for insolvent trading (subject to both criminal and civil penalties). Consequences include civil penalty orders or orders requiring a director to compensate either the company or aggrieved creditors.	
<b>Pending legislation</b>	
None.	

<b>AUSTRIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Insolvency proceedings comprising bankruptcy proceedings, reorganisation proceedings and reorganisation proceedings with self-administration are governed by the Austrian Insolvency Code. The EU Insolvency Regulation will affect cross-border insolvencies.
	<b>Customary kinds of security devices on immovables</b>
	The main type of security on immovables is the mortgage.
	<b>Customary kinds of security devices on moveables</b>
	The possible security devices on moveables are the pledge or the transfer of title. For moveables other than rights, these devices are not very practical. Creditors, however, commonly make use of an assignment of receivables as security.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	There is a complete stay of proceedings on the commencement of insolvency proceedings. Secured creditors can still continue to enforce their rights.
	<b>Duties of the insolvency administrator</b>
	In bankruptcy the insolvency administrator takes control over the debtor's assets and effects the distribution of such assets. In reorganisation proceedings (without self-administration) the insolvency administrator takes control over the debtor's assets and reviews the reorganisation plan. In reorganisation proceedings (with self-administration) the reorganisation administrator supervises the debtor (who generally stays in control of its assets) and reviews the reorganisation plan.
	<b>Set-off and post-filing credit</b>
	Generally, creditors are entitled to exercise their rights of set-off in all types of insolvency proceedings. Claims that are to be compensated must have been compensatable at the opening of the bankruptcy proceedings. In insolvency proceedings an insolvency administrator is entitled to conclude credit agreements on behalf of the insolvent's estate.
	<b>Creditor claims and appeals</b>
	In insolvency proceedings, the creditor must file its claims with the court. If the claim is disputed, the creditor must commence (or continue) legal proceedings to establish its claim, if it had not obtained an enforceable judgment prior to the initiation of the insolvency proceedings.
	<b>Priority claims</b>
	Claims against the debtor that arise from the continuing of business activities or liquidation of the business during the insolvency proceedings are generally granted priority.
<b>Major kinds of voidable transactions</b>	
Under certain preconditions the debtor's transactions are voidable where they give preference to one creditor over others.	
<b>Operating and financing during reorganisations</b>	
In reorganisation proceedings the debtor can continue to operate if and to the extent ordered to do so by the administrator, or, in the case of reorganisation proceedings with self-administration subject to the administrator's supervision. Claims against the debtor arising from the continuation of business during the reorganisation proceedings are granted priority.	
<b>International cooperation and communication</b>	
Austrian law allows for cross-border cooperation in several ways and provides for information transfers to foreign administrators and the foreign administrators right to submit proposals and statements relating to reorganisation plans and the liquidation or utilisation of assets located in Austria.	
<b>Liabilities of directors and officers</b>	
Directors can be personally liable for damage suffered because of the late filing of a petition. Managing directors may be personally liable for taxes and social security contributions.	
<b>Pending legislation</b>	
None.	

<b>BAHAMAS</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Companies (Winding-up Amendment) Act; the Companies Liquidation Rules 2012.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages and fixed charges.
	<b>Customary kinds of security devices on moveables</b>
	Floating charges.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	An automatic stay follows the appointment of a provisional liquidator and the making of a winding-up order by the court.
	<b>Duties of the insolvency administrator</b>
	To collect in the assets of the insolvent and pay out creditors as prescribed by statute.
	<b>Set-off and post-filing credit</b>
	A mandatory set-off arises in an insolvent winding-up. Credit may be obtained for the beneficial winding up of the insolvent.
	<b>Creditor claims and appeals</b>
	Creditors must file claims to prove their debts, which the liquidator must examine. The decision of the liquidator to reject a claim is appealable.
	<b>Priority claims</b>
	Costs and expenses of the winding-up, taxes and statutory charges, employees' wages and amounts due to workmen for personal injuries.
	<b>Major kinds of voidable transactions</b>
	Dispositions after commencement of winding up, fraudulent preferences and transactions at undervalue.
	<b>Operating and financing during reorganisations</b>
	Dependent upon terms of approved plan of arrangement.
<b>International cooperation and communication</b>	
The court is empowered to make wide-ranging ancillary orders in aid of a foreign bankruptcy case.	
<b>Liabilities of directors and officers</b>	
Past and present officers and directors may be compelled to repay monies or contribute to the assets of the company on proof of specified forms of misconduct.	
<b>Pending legislation</b>	
None.	

<b>BAHRAIN</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Law No. 11 of 1987 (the Bankruptcy Law), the Civil Code, the Companies Law and CBB and Financial Institutions Law.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages, pledges and assignments.
	<b>Customary kinds of security devices on moveables</b>
	Pledges, assignments and rights of retention.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Stay of proceedings will come into force upon commencement of any reorganisation proceedings or administration of any financial institution. Stay of proceedings is also applicable in bankruptcy proceedings, but does not extend to secured creditors.
	<b>Duties of the insolvency administrator</b>
	To administer and preserve the debtors funds and act on its behalf in relation to transactions and report to the court.
	<b>Set-off and post-filing credit</b>
	Set-off is exercisable in bankruptcy proceedings if debts are interrelated. Post-credit filing is possible in certain circumstances to the extent necessary.
	<b>Creditor claims and appeals</b>
	Creditors are invited to submit claims upon commencement of insolvency proceedings. Appeals are available.
	<b>Priority claims</b>
	Generally, expenses of insolvency proceedings and taxes owed to government.
	<b>Major kinds of voidable transactions</b>
Transactions that increase financial obligations of the debtor give unjustified preference to creditors. Transactions that are at an undervalue, fraudulent or preferential in the context of financial institutions.	
<b>Operating and financing during reorganisations</b>	
Possible provided it is in the course of business. Approval of the court will be required otherwise.	
<b>International cooperation and communication</b>	
Generally, save for GCC countries, there are no international treaties in place to allow for cooperation between domestic and foreign courts.	
<b>Liabilities of directors and officers</b>	
Directors are liable for fraud and mismanagement. Directors of insolvent financial institutions are liable for carrying on licensed activity when the institution was insolvent.	
<b>Pending legislation</b>	
None that we are aware of.	

<b>BELGIUM</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Bankruptcy: Law of 8 August 1997; Reorganisations: Law of 31 January 2009.
	<b>Customary kinds of security devices on immovables</b>
	The most important form of security is the mortgage.
	<b>Customary kinds of security devices on moveables</b>
	The principal type of security is a pledge. Other types of security: floating charge, statutory lien and retention of title.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Voluntary reorganisation: within 10 days of the debtor's request for the reorganisation, the court may grant a moratorium for a maximum of six months. During this moratorium period, no enforcement can take place in principle against the debtor's assets and no bankruptcy proceedings can be opened. Bankruptcy: All legal proceedings in relation to enforcement will be stayed.
	<b>Duties of the insolvency administrator</b>
	Reorganisation: in case the debtor's obvious and serious defaults are threatening the continuity of his business, every interested party can ask for the appointment of a court representative, whose responsibility will be to file, on behalf of the debtor, a request for a judicial reorganisation procedure and to take any necessary measure to preserve its continuity. Bankruptcy: the bankruptcy trustee's main duty is to liquidate the assets of the debtor to satisfy creditors' claims. The trustee will review creditors' claims and, if he or she disputes them, refer them to the court.
	<b>Set-off and post-filing credit</b>
	Creditors can in certain circumstances exercise their right of set-off provided it was agreed prior to the insolvency and provided further that it relates to mutual debts existing prior to the insolvency. Loans and credit granted after the commencement of liquidation proceedings will receive preferential treatment over other claims if they are considered administrative expenses.
	<b>Creditor claims and appeals</b>
	Bankruptcy: creditors must file their claim at court by the day mentioned in the bankruptcy declaration. If bankruptcy trustee disputes the claim, the court will decide. Decisions can be appealed. Judicial reorganisation: debtors must draw up a list containing all outstanding claims and send this to their creditors, within 14 days after the moratorium period is granted. This information will then be verified by each creditor. In case of disagreement between the creditor and the debtor, the court will resolve such dispute.
	<b>Priority claims</b>
	Basic concept for priority rules is the difference between specific statutory liens and general statutory liens. The former will nearly always rank in priority to the latter.
<b>Major kinds of voidable transactions</b>	
The main voidable transactions are transactions at an undervalue or security arrangements entered into during a 'suspect period' of a maximum of six months preceding a bankruptcy decision, as well as transactions entered into during such period with counterparties that were aware that the debtor was actually insolvent.	
<b>Operating and financing during reorganisations</b>	
The court will in principle allow the debtor to continue to operate the business during the moratorium period. All ongoing contracts will continue notwithstanding the judicial reorganisation.	
<b>International cooperation and communication</b>	
A Belgian bankruptcy trustee will provide information and cross-border cooperation in respect of foreign court proceedings, in accordance with the relevant provisions of the EC Regulation on Insolvency Proceedings (No.1346/2000) and the Belgian private international law code.	
<b>Liabilities of directors and officers</b>	
In general, directors and officers are not liable for the company's debts. They may become liable if, as a result of their obvious default, not all of the company's debts can be paid in full.	
<b>Pending legislation</b>	
A new law governing security interests on moveables has been adopted. Its entry into force will be determined by Royal Decree, but it will enter into force at the latest by 1 January 2017.	

<b>BERMUDA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Companies Act 1981.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages, legal and equitable.
	<b>Customary kinds of security devices on moveables</b>
	Liens, pledges, chattel mortgages and retention of title clauses.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Upon making of a winding-up order or the appointment of provisional liquidator.
	<b>Duties of the insolvency administrator</b>
	Gathering in, preserving assets, adjudicating claims and paying pro rata distributions to admitted creditors.
	<b>Set-off and post-filing credit</b>
	A mandatory set off.
	<b>Creditor claims and appeals</b>
	Upon a notice given to file claims and a 21-day appeal to court.
	<b>Priority claims</b>
	Taxes, workers compensation and employment claims.
	<b>Major kinds of voidable transactions</b>
Fraudulent conveyances within six years, voidable preferences within six months and floating charges if granted within one year of insolvency.	
<b>Operating and financing during reorganisations</b>	
With sanction of the court.	
<b>International cooperation and communication</b>	
Generally, good recognition and foreign liquidators.	
<b>Liabilities of directors and officers</b>	
Fraudulent trading and misfeasance (subject to limitations in by-laws).	
<b>Pending legislation</b>	
None.	

<b>BOTSWANA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Companies Act and the Insolvency Act.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage bonds.
	<b>Customary kinds of security devices on moveables</b>
	Hypothecs, general notarial bonds and pledges.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Winding up proceedings stays all legal action unless the prior leave of court has been sought and obtained.
	<b>Duties of the insolvency administrator</b>
	A liquidator essentially replaces the insolvent and performs all the obligations that the insolvent would have otherwise been obliged to perform.
	<b>Set-off and post-filing credit</b>
	Set-off can occur prior to the sequestration provided the creditor claiming the benefit did not know of the impending insolvency.
	<b>Creditor claims and appeals</b>
	All claims must be submitted to the master and liquidator to be proofed. A creditor whose claim is rejected is at liberty to institute legal proceeding against the liquidator for relief.
	<b>Priority claims</b>
	Secured claims are paid first, followed by preferent claims and then concurrent claims are last in line.
<b>Major kinds of voidable transactions</b>	
Payments received immediately before the sequestration that has the effect of preferring one creditor over the others.	
<b>Operating and financing during reorganisations</b>	
The costs of the sequestration are usually considered as administrative costs and are paid prior to any other distribution being made.	
<b>International cooperation and communication</b>	
None that we are aware of.	
<b>Liabilities of directors and officers</b>	
Directors of companies who continue to incur liabilities for the insolvent in the full knowledge that the insolvent is unable to meet its payment obligations as and when they fall due for payment become personally liable for the obligations created.	
<b>Pending legislation</b>	
We are not aware of any such pending legislation.	

<b>BRAZIL</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Federal Law No. 11.101/2005, applicable to judicial reorganisation, out-of-court reorganisation and forced liquidation proceedings.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage and fiduciary sale.
	<b>Customary kinds of security devices on moveables</b>
	Pledge and fiduciary transfer.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	180 days in judicial reorganisation proceedings; indefinitely in forced liquidation proceedings; or applicable to claims with no predetermined amount.
	<b>Duties of the insolvency administrator</b>
	Depends on the proceeding. In a judicial reorganisation, analyse the creditors' claims and consolidate the list of creditors, provide monthly reports of the debtor company's activities and supervise the debtor company's activities. In forced liquidation proceedings, analyse the creditors' claims and consolidate the list of creditors, collect and sell the assets, distribute the proceeds of the assets sale among creditors, according to legal order of payment. Always provide information requested by the court or by creditors.
	<b>Set-off and post-filing credit</b>
	Set-off is possible in forced liquidation proceedings but, in principle, are not possible in judicial reorganisations. In judicial reorganisations, credits that are post-filing are not affected by the proceeding and may be enforced.
	<b>Creditor claims and appeals</b>
	Creditors are given the opportunity of presenting statement of credit to the judicial administrator and proof of claim to the bankruptcy court, and are able to appeal from several decisions.
	<b>Priority claims</b>
	Labor claims up to 3 minimum wages; judicial administrator fees; sums provided to the bankruptcy estate by the creditors; expenses with schedules, management, asset sale and distribution of the proceeds; court costs of the forced liquidation proceedings; court costs with respect to actions and enforcement suits found against the bankruptcy estate; obligations resulting from valid legal acts performed and contracts agreed during the judicial restructuring proceeding, or after the decree of the forced liquidation, and taxes relating to triggering events postdating the decree of the forced liquidation.
	<b>Major kinds of voidable transactions</b>
Payment of unmatured debts during the suspect period; payment of overdue debts effected during the suspect period in a manner that is different from what was established in the original agreement; the creation of security interests during the suspect period to secure payment of pre-existing indebtedness; donations and other equivalent actions effected within the period of 2 years preceding the forced liquidation; any action aimed at intentionally defrauding creditors.	
<b>Operating and financing during reorganisations</b>	
It is allowed and given priority in case of forced liquidation.	
<b>International cooperation and communication</b>	
No provision in the BRL.	
<b>Liabilities of directors and officers</b>	
In forced liquidation proceedings, shareholders, controlling shareholders, directors and executive officers may be considered liable for debts and/or acts liabilities if the bankruptcy court verifies that they performed any act or omission that contravenes Brazilian Law, regardless of the collection of the assets and impossibility to pay all the creditors of the company; possibility of disregard of corporate veil.	
<b>Pending legislation</b>	
Legislative Bill No. 314/2014 - alteration of the name of the law. Legislative Bill No. 5587/2013 - regulation of the extension of the bankruptcy effects to affiliated companies and companies controlled by the debtor	

<b>BULGARIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Commerce Act, Bank Insolvency Act, Credit Institutions Act, Insurance Code, Social Security Code, Council Regulation No. 1346/2000 of 29 May 2000.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage and special pledge.
	<b>Customary kinds of security devices on moveables</b>
	Common and special pledge.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	All judicial and arbitration proceedings brought against the debtor except for those explicitly listed in the Commercial Act.
	<b>Duties of the insolvency administrator</b>
	Representation of the enterprise, administration of its current affairs, supervision over the activities of the debtor, identification and establishment of the debtor's assets, cancellation or invalidation of contracts, participation in judicial proceedings and bringing lawsuits, identification of debtor's creditors, convening of meetings of the creditors, conversion of the insolvency estate into cash, etc.
	<b>Set-off and post-filing credit</b>
	Allowed under specific conditions.
	<b>Creditor claims and appeals</b>
	Creditors submit their claims before the insolvency court. A creditor may file a written objection before the court against any claim admitted or rejected by the insolvency administrator.
	<b>Priority claims</b>
	The creditors are divided into three categories according to the type of their claims: secured, unsecured and creditors whose claims are satisfied following the full satisfaction of the rest of the creditors. All claims are arranged in rank in accordance with the order of claims prescribed by the Commerce Act.
	<b>Major kinds of voidable transactions</b>
Actions and transactions which harm the amount of the insolvency estate by decreasing it.	
<b>Operating and financing during reorganisations</b>	
In general under the supervision of the insolvency administrator and the meeting of the creditors.	
<b>International cooperation and communication</b>	
European Council Regulation No. 1346/2000 of 29 May 2000.	
<b>Liabilities of directors and officers</b>	
Civil and penalty liability for the nonfulfillment of the prescriptions of the acting Bulgarian insolvency legislation.	
<b>Pending legislation</b>	
The legal system of Bulgaria is in the process of unifying with European and world standards in insolvency proceedings.	

<b>CANADA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Bankruptcy and Insolvency Act (BIA) (used for liquidations and smaller reorganisations) and Companies' Creditors Arrangement Act (CCAA) (used for larger commercial reorganisations). Insolvencies of banks, insurance companies and significant financial institutions are dealt with under the Federal Winding-up and Restructuring Act (WURA).
	<b>Customary kinds of security devices on immovables</b>
	Mortgages (liens or charges) that are registered on immovable property in the public land registration office in the province where the immovable is located.
	<b>Customary kinds of security devices on moveables</b>
	'Security interests' on moveables under personal property security legislation have replaced chattel mortgages, conditional sales (hire-purchase) agreements and assignments of book debts, although some of these terms are still used to describe their particular form of security interest.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Reorganisations: BIA stays against secured and unsecured creditors' claims are automatic on filing. Courts can lift the stays in cases of unfairness. CCAA stays are broader and are created by court order when CCAA protection is granted. Liquidations: stays of proceedings by unsecured creditors and limited stays of proceedings against secured creditors.
	<b>Duties of the insolvency administrator</b>
	Reorganisations: a 'proposal trustee' under the BIA and a 'monitor' under the CCAA are appointed in all cases and review the financial condition of the debtor, administer the claims-proving process and carry out distributions under the proposal (BIA) or plan (CCAA). Liquidations: a BIA bankruptcy trustee is vested with the debtor's unencumbered property, collects and disposes of assets, supervises the claims-proving process and distributes funds to creditors.
	<b>Set-off and post-filing credit</b>
	Rights of set-off are preserved in the BIA. They are restrained in CCAA reorganisations but are customarily recognised in CCAA plans. Netting is specifically preserved for eligible financial contracts in both the BIA and the CCAA. Post-commencement financing is authorised under the BIA and the CCAA, and the court may allow it to prime (ie, have priority over) existing security. Existing pre-filing secured claims continue to apply to the assets of a reorganising business. There is no general administrative expense priority in either the BIA or the CCAA although court orders occasionally permit it. Both the BIA and the CCAA permit suppliers to require COD or cash terms. Under the CCAA, the court may, on suitable terms, compel a critical supplier to continue to supply.
	<b>Creditor claims and appeals</b>
	Proofs of claim must be filed by both secured and unsecured creditors. Claims may be disallowed by the trustee (BIA) or monitor (CCAA). Disallowances can be appealed to the court within a limited time frame.
	<b>Priority claims</b>
	Governmental claims for statutory deductions from employees' wages are given priority over all other claims including secured claims on moveables (but not over charges on immovables). New legislation provides for limited super-priority for employee wage arrears and unlimited super-priority for pension contribution arrears. Limited supplier reclamation rights are available for goods supplied shortly before bankruptcy, but are not very effective. There is no express administrative expense priority in reorganisations. Preferred claims include costs of administration and up to three months' rent for landlords.
<b>Major kinds of voidable transactions</b>	
Preferences (transactions made by the debtor with the intent of preferring some creditors over others) within three months of bankruptcy (for arm's-length creditors) or, (in the case of transactions with non-arm's length creditors) within 12 months of bankruptcy where the effect of the transaction is to prefer the creditor; transfers at undervalue (ie, for less than fair market value); unperfected security interests; dividends issued by insolvent debtor corporations and, under most provincial legislation, transactions that are intended to defeat creditors' claims.	
<b>Operating and financing during reorganisations</b>	
The debtor generally maintains management control subject to review by a proposal trustee (BIA) or a monitor (CCAA) and supervision by the court. The BIA and CCAA now provide for post-filing financing for reorganising debtors, similar to US debtor-in-possession financing, which may rank in priority over existing security. Sale of assets BIA: in liquidations, the trustee can sell assets with approval of the inspectors. In reorganisations, sales of assets out of the ordinary course of business require court approval. CCAA: court orders govern the sales of assets. Sales out of the ordinary course of business require court approval.	
<b>International cooperation and communication</b>	
Canada has adopted the general framework of the UNCITRAL Model Law and has applied it successfully in a large number of cross-border cases. Canadian courts have communicated with foreign courts in international cases for many years.	
<b>Liabilities of directors and officers</b>	
General corporate duty to act honestly and in good faith with fiduciary obligations to the company. Specific statutory liabilities for unpaid employees' wages, certain unremitted employee tax collections and dividends issued while insolvent. Numerous other corporate liabilities to governmental agencies can crystallise into personal liabilities of directors. There can be significant exposure to environmental liabilities.	
<b>Pending legislation</b>	
Several significant changes to the BIA and the CCAA became effective in September 2009.	

<b>CAYMAN ISLANDS</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Companies Law (2016 Revision); Companies Winding Up Rules, 2008 (as amended).
	<b>Customary kinds of security devices on immoveables</b>
	Registered charge.
	<b>Customary kinds of security devices on moveables</b>
	Mortgages, fixed and floating charges, liens, pledges, retention of title clause.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Court permission is required to commence or continue proceedings against a company in respect of which a winding-up order has been made. After commencement of insolvency proceedings but before winding-up order is made, the company, or a creditor or member may apply for order staying continuation or restraining commencement of proceedings against the company.
	<b>Duties of the insolvency administrator</b>
	Collect and realise assets; adjudicate claims and make distributions to creditors; report on conduct of liquidation.
	<b>Set-off and post-filing credit</b>
	Automatic set-off in insolvency, subject to contractual disapplication and notice of commencement of liquidation.
	<b>Creditor claims and appeals</b>
	Proof of debt with supporting evidence submitted to liquidator. If claim rejected entirely or in part by liquidator, appeal to court within 21 days of notification.
	<b>Priority claims</b>
	Employee-related claims, debts due to bank depositors, taxes due to the government.
	<b>Major kinds of voidable transactions</b>
Voidable preference; transaction at undervalue.	
<b>Operating and financing during reorganisations</b>	
Subject to terms of restructuring plan.	
<b>International cooperation and communication</b>	
Courts generally willing to cooperate with foreign courts, and to recognise or assist foreign insolvency representatives.	
<b>Liabilities of directors and officers</b>	
None, unless personally guaranteed or breached duties.	
<b>Pending legislation</b>	
Not applicable.	

<b>CHINA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Enterprise Bankruptcy Law of the People's Republic of China; the Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the PRC and the Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the PRC II.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage.
	<b>Customary kinds of security devices on moveables</b>
	Mortgage, pledge and lien.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Civil litigation, arbitration, enforcement and preservation measures.
	<b>Duties of the insolvency administrator</b>
	Manage and dispose assets, review creditors' claims, take over financial statements and other documents, timely report to the creditors' committee or to the court.
	<b>Set-off and post-filing credit</b>
	Certain post-filing claims are costs of bankruptcy proceedings or debts for common benefit; set-off is generally allowed with some restrictions.
	<b>Creditor claims and appeals</b>
	Creditor should declare credits within the period designated by the court but supplemental declaration is allowed before the final distribution; creditor may lodge civil action to challenge the claims confirmed by the administrator.
	<b>Priority claims</b>
	Costs of bankruptcy proceedings, debts for common benefit, certain employment-related claims, and certain social security premium claims and claims of taxes.
	<b>Major kinds of voidable transactions</b>
	Transfer of assets free of charge, transaction at an obviously unreasonable price, providing security for unsecured debt, discharge of debt before it is due, and waiver of creditor's claims, within the suspected period of one year; individual repayment when insolvent within the suspected period of six months.
	<b>Operating and financing during reorganisations</b>
Debtor (upon approval) or administrator is responsible for implementing the reorganisation plan; financing during reorganisation is allowed.	
<b>International cooperation and communication</b>	
Bilateral treaty on judicial assistance of civil and commercial matters between China and certain foreign countries.	
<b>Liabilities of directors and officers</b>	
Liable if their breach of fiduciary duties results in the debtor's bankruptcy.	
<b>Pending legislation</b>	
The Provisions on Several Issues Concerning the Application of the Enterprise Bankruptcy Law of the PRC III by the Supreme Court.	

<b>CROATIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Bankruptcy Act. The Act on the Bankruptcy of Consumers. The Enforcement Act. The Companies Act.
	<b>Customary kinds of security devices on immoveables</b>
	Pledge. Fiduciary transfer of ownership.
	<b>Customary kinds of security devices on moveables</b>
	Pledge.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Generally, initiation of bankruptcy or pre-bankruptcy proceedings causes stay of most proceedings concerning the debtor.
	<b>Duties of the insolvency administrator</b>
	Draw up the initial state of the debtor's assets. Manage the business operations of the debtor. Prepare the bankruptcy plan. Cash in the bankruptcy estate. Draw up final accounts.
	<b>Set-off and post-filing credit</b>
	Set-off generally allowed. Post-filing credit generally allowed, under prescribed procedure.
	<b>Creditor claims and appeals</b>
	Allowed both in pre-bankruptcy and bankruptcy proceedings.
	<b>Priority claims</b>
	Secured assets and excluded assets. Expenses of the bankruptcy estate. Claims of employees.
	<b>Major kinds of voidable transactions</b>
	Transaction causing creditors damage or preferential treatment of certain creditors.
	<b>Operating and financing during reorganisations</b>
	In pre-bankruptcy proceedings – debtor conducting business under supervision, in bankruptcy proceedings – bankruptcy administrator conducting business.
<b>International cooperation and communication</b>	
Allowed.	
<b>Liabilities of directors and officers</b>	
When not submitting a required proposal for the opening of the bankruptcy proceedings and when not using care of a diligent and conscientious business.	
<b>Pending legislation</b>	
None.	

<b>CYPRUS</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Bankruptcy Law. Companies Law. Insolvency of Individuals (Personal Repayment and Relief Plans) Law 65(I)/2015.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages (legal and equitable). Memoranda on immoveable property.
	<b>Customary kinds of security devices on moveables</b>
	Pledge, floating charge, fixed charge, lien, retention of title clauses (Romalpa clauses) and ship mortgages.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Following appointment of a liquidator no action or proceedings shall be made against the company (except under court leave); and During the duration of examinership, there can be no action taken against a company.
	<b>Duties of the insolvency administrator</b>
	Depending on whether it concerns examinership or liquidation, the Insolvency administrator is under the duty to liquidate the company and sell all assets in the best interests of the creditors (as a class) and to handle all affairs of the company until its dissolution (liquidation). In examinership, the insolvency administrator has the aim to complete the examinership and keep the company alive and make an arrangement with its creditors so that it is made sustainable.
	<b>Set-off and post-filing credit</b>
	Permitted and handled at the discretion of the liquidator under the provisions relating to preferential treatment of creditors and aiming to secure the best deal for the company.
	<b>Creditor claims and appeals</b>
	Creditors need to provide the liquidator with their claim against the company following the publishing of the liquidators appointment. Appeals against action of the liquidator can be made to court and the court will examine the request by the creditor.
	<b>Priority claims</b>
	Priority claims as follows: <ul style="list-style-type: none"> <li>• costs of winding up</li> <li>• preferential debts as outlined in the law (taxes, unpaid wages and certain compensations);</li> <li>• secured creditors;</li> <li>• unsecured ordinary creditors;</li> <li>• deferred debts; and</li> <li>• any surplus will be distributed among the members of the company.</li> </ul>
	<b>Major kinds of voidable transactions</b>
	All transactions six months prior to liquidation may be considered as preferential treatment to creditors (fraudulent preference) and may be annulled.
	<b>Operating and financing during reorganisations</b>
Individuals may obtain credit in bankruptcy only if they inform the creditor that they are insolvent. Companies during examinership may operate as usual and may obtain credit (such credit will rank above all other creditors) upon approval by the examiner.	
<b>International cooperation and communication</b>	
No cross-border handling of cases. Bound by EU Regulations on Insolvency Proceedings.	
<b>Liabilities of directors and officers</b>	
Liabilities if trading while company is insolvent. Liability for transactions made in the six months prior to liquidation, if found to be made for the purpose of preferential treatment of creditors.	
<b>Pending legislation</b>	
The insolvency regime (both corporate and personal) in Cyprus has been revised and updated while it has introduced new concepts for bankruptcy protection under examinership and for the protection of insolvent individuals. These revisions have been implemented in the past year (2015) and no further major revisions of the law or new legislation are expected within the next year.	

<b>DOMINICAN REPUBLIC</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Dominican Code of Commerce and Law No. 4582 of 1956. A new Law on Restructuring and Liquidation of Companies and Business Persons (Law No. 141-15), was enacted on 7 August 2015 and will enter into effect on 7 February 2017 (18 months after its enactment).
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages.
	<b>Customary kinds of security devices on moveables</b>
	Non-possessory pledges; ordinary civil and commercial pledges, mostly for intangibles.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Upon initiation of the conciliation and negotiation process, all judicial, administrative or arbitral decisions that affect the assets of the debtor and any enforcement or eviction procedures regarding the debtor's property (moveable and immoveable) are suspended until the reorganisation plan is approved, or until the judgment that orders a judicial liquidation is rendered.
	<b>Duties of the insolvency administrator</b>
	During the restructuring phase, the principal role of the conciliator is to mediate between the debtor and its creditors in order to reach a restructuring plan. The management of the debtor's assets continues to be handled by the debtor, but remains subject to the supervision of the conciliator. During the liquidation phase, the liquidator assumes all management functions and powers of the debtor.
	<b>Set-off and post-filing credit</b>
	Permitted with court approval except for claims not yet due and payable.
	<b>Creditor claims and appeals</b>
	15 days after notice of proceedings and possibility of a 20-day extension following notice in national newspapers; contested claims are subject to separate judicial proceedings.
	<b>Priority claims</b>
	New debts have a higher priority in relation to all other secured and unsecured claims of the debtor, with the exception of tax claims, employee claims, and claims resulting from the payment of the restructuring process, which are entitled to a higher priority status.
	<b>Major kinds of voidable transactions</b>
	Transfers of assets free of charge or at a price below market value; when the intended consideration is worth less than the obligation performed, or vice versa; the cancellation or partial or total relief of debt by the debtor; the grant of guarantees or the increase of the value of guarantees approved prior to the initiation of the proceeding without reasonable consideration; payments of obligations not yet due; transfers of property in favour of creditors which result in the payment of a higher amount to that received as a result of the liquidation; transactions with related entities.
	<b>Operating and financing during reorganisations</b>
New financing must have the approval of the court and the petition presented by the conciliator may be objected by the creditors. The constitution of new financial collateral may also be authorised by the court, after hearing the creditors' adviser. New obligations will be ranked after existing privileges.	
<b>International cooperation and communication</b>	
New Law No. 141-15 sets forth a legal framework applicable to insolvency proceedings with international or cross-border effects, developed in accordance with the United Nations Commission on International Trade Law (UNCITRAL). The Law provides the recognition of foreign proceedings by local courts, and contemplates the possibility of processing local and foreign insolvency proceedings simultaneously.	
<b>Liabilities of directors and officers</b>	
Corporate officers and directors may be liable for labour claims and tax claims. Their liability may also be established upon their violation of criminal provisions relating to bankruptcies. The officers in charge of the restructuring or liquidation procedures who fail to meet the requirements established by law for the execution of their duties, may face criminal prosecution and be subject to imprisonment and fines.	
<b>Pending legislation</b>	
Law No. 141-15 will enter into effect on 7 February 2017, 18 months after its enactment.	

ENGLAND & WALES	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Principal legislation: Insolvency Act 1986. Subordinate legislation: Insolvency Rules 1986 Other relevant legislation: Company Directors Disqualification Act 1986 and Companies Act 2006, the Financial Collateral Arrangements (No. 2) Regulations 2003 (SI 2003/3226), the EC Insolvency Regulation (and in due course its recast) and the Cross-Border Insolvency Regulations 2006 affect cross-border insolvencies.
	<b>Customary kinds of security devices on immovables</b>
	Principal type of security: legal mortgage (conveyance or assignment of the whole of the legal ownership). Other types of security: equitable mortgage (transfer of beneficial interest only) and fixed charge.
	<b>Customary kinds of security devices on moveables</b>
	Principal types of security: mortgages, fixed charges, floating charges, pledges, liens.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Voluntary liquidations: No automatic moratorium on proceedings against company. Involuntary liquidations: Once order for liquidation has been made, no action can be started or proceeded against the company, without the permission of the court. Administration: Automatic moratorium on proceedings against company and enforcement of security. Reorganisations: No moratorium unless company also in administration (subject to potential new restructuring plan and restructuring moratorium). Potential 28-day moratorium for small companies putting a CVA together.
	<b>Duties of the insolvency administrator</b>
	Liquidation: Liquidator will realise and distribute assets in accordance with distribution priority rules in insolvency. Administration: Administrator has the power to carry on the business of the company and sell its assets where likely to promote purposes of the administration. Administrator may also make distributions. Administrative receivership: Administrative receiver will realise assets to satisfy secured creditor's claim.
	<b>Set-off and post-filing credit</b>
	Legal and equitable set-off rules apply to administrations before a notice of intended distribution is given, receiverships and voluntary arrangements and are confined to money obligations between the insolvent company and the creditor. Insolvency set-off operates in liquidations and administrations once the administrator has given a notice of his intention to make a distribution and applies to mutual dealings between a creditor and the company. A liquidator or administrator can raise money, secured on the company's assets. Such credit has priority over ordinary unsecured creditors only in respect of the new funds. New loans or security will not be capable of taking priority over pre-existing secured debt unless this is permitted under the terms of the pre-existing secured indebtedness. Expenses of the administration (or liquidation) will rank ahead of floating charges.
	<b>Creditor claims and appeals</b>
	Creditors submit claims to liquidator and administrator by way of 'proof of debt'. Time limits may be set before interim dividends paid. Creditor can appeal to court against a rejection of its proof within 21 days.
	<b>Priority claims</b>
	There are comparatively few types of preferential claims. The main ones are occupational pension schemes in respect of unpaid contributions and employees who are owed remuneration up to a set amount. In relation to a financial institution, certain debts in relation to the Financial Services Compensation Scheme will also rank as preferential claims. The expenses of preserving and realising the assets, including the costs and expenses of the various office holders will also take priority over certain groups of creditors. In a reorganisation the order of priority will be a matter of negotiation between the parties.
	<b>Major kinds of voidable transactions</b>
Transactions at an undervalue, preferences, certain floating charges granted in suspect period.	
<b>Operating and financing during reorganisations</b>	
In an administration the directors' powers cease (although they remain in office) and the administrator has the power to carry on the business of the company and to sell its assets. In a scheme and CVA the directors remain in control.	
<b>International cooperation and communication</b>	
Section 426 of the Insolvency Act, the EC Regulation (and in due course its recast) and the Cross-Border Insolvency Regulations work in parallel, together with common law principles of comity and to a certain extent, modified universalism.	
<b>Liabilities of directors and officers</b>	
Misfeasance or breach of fiduciary or other duty, fraudulent trading, wrongful trading.	
<b>Pending legislation</b>	
A major revision of the Insolvency Rules 1986 is expected in autumn 2016 to take effect in 2017. Major reform will be required in connection with the UK's exit from the EU.	

<b>EUROPEAN UNION</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Until 25 June 2017: EC Regulation on Insolvency Proceedings 2000. After 26 June 2017: recast to the EC Regulation. Other relevant legislation: Credit Institutions Directive, Insurance Undertakings Directive, Bank Recovery and Resolution Directive, Financial Collateral Arrangements Directive.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages and fixed charges (but no EU-wide harmonised system).
	<b>Customary kinds of security devices on moveables</b>
	Security assignments, fixed charges, floating charges, pledges, liens (but no EU-wide harmonised system).
	<b>Stays of proceedings in reorganisations/liquidations</b>
	This is a matter for the law of the member state in which those proceedings are opened.
	<b>Duties of the insolvency administrator</b>
	The duties of the insolvency office holder will depend on the type of insolvency procedure the debtor is undergoing.
	<b>Set-off and post-filing credit</b>
	Set off: The conditions under which set-offs may be invoked are determined by the laws of the member state in which proceedings are opened. The opening of insolvency proceedings must not affect the right of creditors to demand set-off of a creditor's claims against the claims of the debtor, where such a set-off is permitted by the law applicable to the debtor's claim. Post-filing credit: procedures vary significantly between jurisdictions.
	<b>Creditor claims and appeals</b>
	Creditors submit claims to liquidator and administrator by way of 'proof of debt'. Time limits may be set before interim dividends paid. Creditors can appeal to court against a rejection of its proof within 21 days.
	<b>Priority claims</b>
	Most jurisdictions afford some measure of priority for certain tax and other governmental claims. In some jurisdictions there is a requirement for money to be ring-fenced for employees. Most jurisdictions also provide that the costs of an insolvency process and the insolvency office holder's fees and expenses are paid out first.
	<b>Major kinds of voidable transactions</b>
	The rules are a matter for the law of the state where the insolvency proceedings are opened.
	<b>Operating and financing during reorganisations</b>
	The rules vary among member states. Where a reorganisation is implemented under the supervision of the court a debtor will be able to carry on its business subject to court-imposed conditions. The powers that directors and officers can exercise after insolvency proceedings have been commenced vary according to both the type of insolvency process and member state.
<b>International cooperation and communication</b>	
The EC Regulation (and in due course its recast) governs cross-border insolvency proceedings for member states. The UNCITRAL Model Law on Cross-Border Insolvency has currently only been implemented by Greece, Poland, Romania, Slovenia and the United Kingdom. Office holders in main proceedings and secondary proceedings have a duty to communicate and cooperate.	
<b>Liabilities of directors and officers</b>	
The laws governing liability will generally be those of the jurisdiction of incorporation, where insolvency proceedings are commenced in that jurisdiction. Generally, directors and officers may be liable to contribute to the debtor's assets, but this is normally limited to where conduct falls below the requisite standard. Directors are also exposed to a range of criminal sanctions arising from their conduct prior to insolvency.	
<b>Pending legislation</b>	
The Commission intends to present a legislative proposal on insolvency by the end of 2016. EU legislation as it applies to the EU member states will be unaffected by Brexit (unless as part of the Brexit negotiations, legislation is amended to cater for Brexit).	

<b>FRANCE</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Codified in the French Commercial Code at article L610-1 et seq.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages.
	<b>Customary kinds of security devices on moveables</b>
	Pledges.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	A stay of proceedings is applicable from the date of the judgment opening safeguard, reorganisation or liquidation proceedings.
	<b>Duties of the insolvency administrator</b>
	To supervise, assist or replace the management in place depending on the type of insolvency proceedings or the situation at stake.
	<b>Set-off and post-filing credit</b>
	Set-off between a pre-filing and a post-filing credit is possible in limited circumstances.
	<b>Creditor claims and appeals</b>
	Creditors generally have two months (+ two months for foreign creditors) from the date the judgment ordering the opening of the insolvency proceedings to send a statement of their claim to the court-appointed creditors' representative. In certain circumstances, creditors enjoy a right of appeal and opposition to insolvency judgments.
	<b>Priority claims</b>
	Certain claims enjoy a priority repayment, namely certain employee-related claims, tax claims and claims resulting from new money or goods provided for the debtor company in a conciliation.
	<b>Major kinds of voidable transactions</b>
Transactions entered into during the 'suspect period' - the period between the date on which the debtor is deemed to have become insolvent and the date on which the insolvency proceedings are opened - may be declared null and void.	
<b>Operating and financing during reorganisations</b>	
New financing granted to a company in conciliation or insolvency proceedings will enjoy a priority repayment.	
<b>International cooperation and communication</b>	
Cooperation between insolvency practitioners usually results in the signing of cooperation protocols.	
<b>Liabilities of directors and officers</b>	
Directors and officers can be held personally liable for all or part of the debts of the company placed in liquidation proceedings if they are found to have mismanaged the company's business. In limited circumstances, directors and officers can also be held criminally liable.	
<b>Pending legislation</b>	
Not applicable.	

<b>GERMANY</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The German Insolvency Act. The adopted EU Insolvency Regulation affects cross-border insolvencies.
	<b>Customary kinds of security devices on immoveables</b>
	<i>Hypothek</i> : charge on real property as security for payment of a certain sum that equals the secured personal debt. <i>Grundsschuld</i> : charge on real property for payment of a definite sum of money.
	<b>Customary kinds of security devices on moveables</b>
	Retention of title; fiduciary transfer of assets; fiduciary transfer of receivables; and chattel pledge.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	For the duration of insolvency proceedings, claims cannot be enforced by individual insolvency creditors (save for enforcement actions by secured creditors). The insolvency court may prohibit or suspend measures of execution against the debtor's assets for the period between the application for the opening of insolvency proceedings and the ruling on the application.
	<b>Duties of the insolvency administrator</b>
	The administrator (in both liquidations and reorganisations) takes possession of and administers all assets that comprise the insolvency estate. The powers of the debtor's management pass to the administrator.
	<b>Set-off and post-filing credit</b>
	Generally, claims by or against the insolvency estate existing as of the date of the opening of the insolvency proceedings may be set off against each other, provided that the set-off position has been created prior to the opening. If a debt is to be incurred that would significantly burden the insolvency estate, the insolvency administrator must obtain the consent of the creditors' meeting. Besides this, an insolvency plan can give priority to creditors that make loans or other credits available to the debtor or a takeover company.
	<b>Creditor claims and appeals</b>
	Creditors must submit their claims to the administrator within a period set by the court between two weeks and three months from the date of the order opening the insolvency procedure. If the claim is disputed by the administrator or another creditor, the creditor can issue an appeal.
	<b>Priority claims</b>
	Creditors with proprietary claims for the return of assets not belonging to the insolvency estate are not affected by the insolvency. Costs of the insolvency rank in priority over unsecured creditors.
	<b>Major kinds of voidable transactions</b>
	The administrator may set aside transactions that prefer one creditor over another or where there has been a fraudulent conveyance. The repayment of shareholder loans made within the last year prior to the filing for the opening of insolvency proceedings is voidable.
	<b>Operating and financing during reorganisations</b>
	The right to manage and transfer the debtor's assets passes to the administrator upon the opening of the insolvency proceedings. The debtor may apply to court for self-management under an insolvency practitioner's supervision.
<b>International cooperation and communication</b>	
A German administrator shall share all relevant information and documentation with a foreign administrator in order to facilitate an effective and smooth process and the best possible satisfaction of creditors in the insolvency procedures. Although there is no specific statutory duty, German insolvency courts usually cooperate with foreign insolvency courts in order to avoid jurisdictional conflicts.	
<b>Liabilities of directors and officers</b>	
The managing directors of a German limited liability company and the members of the management board of a stock corporation may have a (personal) liability to third parties and the company itself. In particular, such liability may result from the delayed application for the opening of insolvency proceedings or an action that leads to a reduction of the (insolvency) estate.	
<b>Pending legislation</b>	
In January 2014, the German government passed an official legislative draft bill that aims to facilitate the handling of group insolvencies. In September 2015, the German Federal Ministry of Justice issued a (revised) draft reform act on insolvency avoidance law	

<b>GREECE</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Law No. 3588/2007, as amended. Law No. 3858/2010. The EC Regulation.
	<b>Customary kinds of security devices on immoveables</b>
	Prenotation of mortgage. Mortgage.
	<b>Customary kinds of security devices on moveables</b>
	Pledge. Notional pledge. Floating charge. Retention or fiduciary transfer of ownership. Third-party structure.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Automatic stay upon commencement of bankruptcy proceedings. Stay upon application in recovery and special liquidation proceedings. Automatic stay upon application of pre-packaged recovery process.
	<b>Duties of the insolvency administrator</b>
	Management of the insolvency estate.
	<b>Set-off and post-filing credit</b>
	Yes provided that the claim fell due prior to the declaration of bankruptcy. The claims that arise from post-plan ratification financing are ranked ahead of any other pre-existing claim.
	<b>Creditor claims and appeals</b>
	Announcement of creditors' claims. Appeal against the judgment that accepts or rejects a creditor's claim.
	<b>Priority claims</b>
	The following creditors' claims are ranked at the same class: <ul style="list-style-type: none"> <li>• unpaid employee remuneration incurred in the two years prior to bankruptcy being declared and employment termination compensation;</li> <li>• lawyers' fees that date up to six months prior to the declaration of bankruptcy, and claims for compensation of salaried lawyers because of termination of their contract for a salaried mandate;</li> <li>• social security contributions that arose until the declaration of bankruptcy; and</li> <li>• Claims of the state arising from value added tax (VAT) and its surcharges.</li> </ul> Other claims of the state excluding claims arising from VAT.
	<b>Major kinds of voidable transactions</b>
<ul style="list-style-type: none"> <li>• Donations and gratuitous acts;</li> <li>• payments of debts that did not fall due;</li> <li>• payments of due debts that were not made in cash; and</li> <li>• security over the debtor's estate for pre-existing debts.</li> </ul>	
<b>Operating and financing during reorganisations</b>	
Upon declaration of bankruptcy, the bankruptcy administrator manages the debtor's assets and affairs. Upon application, the court may permit the debtor to remain in administration of its assets always along with the bankruptcy administrator's cooperation.	
<b>International cooperation and communication</b>	
Law No. 3858/2010. The EC Regulation.	
<b>Liabilities of directors and officers</b>	
The general partner of a limited partnership: personally liable for corporate debts. Directors and officers of a limited liability company and a société anonyme: in principle, no liability. Exceptions are: <ul style="list-style-type: none"> <li>• personal liability in the event of delay with regard to the filing of the bankruptcy petition; or fraudulent act or gross negligence; and</li> <li>• personal and joint liability with regard to the payment of corporate taxes.</li> </ul>	
<b>Pending legislation</b>	
Not applicable.	

<b>HONG KONG</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Companies (Winding Up and Miscellaneous Provisions) Ordinance, Companies Ordinance, Bankruptcy Ordinance, Banking Ordinance, subsidiary legislation.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages and charges.
	<b>Customary kinds of security devices on moveables</b>
	Mortgages. Charges (fixed and floating). Pledges. Liens. Quasi-security (eg, set-off and retention of title arrangements).
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Discretionary stay with court leave of legal actions and enforcement procedures after petition presented. Absolute stay absent court leave when provisional liquidator appointed or winding-up order made. No statutory stay in reorganisations.
	<b>Duties of the insolvency administrator</b>
	Duties of a liquidator: <ul style="list-style-type: none"> <li>• to receive statement of affairs;</li> <li>• to adjudicate on creditors' claims;</li> <li>• to collect and preserve debtor's assets; and</li> <li>• to realise the debtor's assets and to distribute dividends to creditors.</li> </ul> Duties of a receiver: <ul style="list-style-type: none"> <li>• to realise secured assets for charge holder; and</li> <li>• to return surplus assets to company.</li> </ul>
	<b>Set-off and post-filing credit</b>
	Generally there is automatic and mandatory set-off of mutual credits, mutual debts and other mutual dealings.
	<b>Creditor claims and appeals</b>
	Creditors file proof of debts with liquidator. Rejections can be appealed to the High Court.
	<b>Priority claims</b>
	Costs and expense of the insolvency proceedings. Creditors secured by a fixed charge. Preferential creditors (eg, employees, Hong Kong government). Creditors secured by a floating charge. Unsecured creditors.
	<b>Major kinds of voidable transactions</b>
	Unfair preferences, fraudulent dispositions/conveyance and invalid floating charges. Currently, no transaction-at-an-undervalue provisions.
	<b>Operating and financing during reorganisations</b>
	Currently no statutory reorganisation procedure. Directors remain in control until a provisional liquidator or liquidator is appointed to the company. No special financing regime during reorganisation.
<b>International cooperation and communication</b>	
Principles based on comity have evolved to guide the practical coordination of Hong Kong and foreign proceedings.	
<b>Liabilities of directors and officers</b>	
Fraudulent trading. Misfeasance. Falsification or destruction of books and records. Disqualification of directors.	
<b>Pending legislation</b>	
Legislation is expected to be introduced in respect of both special resolution regimes for financial institutions and insolvency reform generally. It is likely that the latter will introduce, inter alia, a provisional supervision regime, insolvent trading provisions and the power for the court to unwind transactions at an undervalue.	

<b>HUNGARY</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Act XLIX of 1991 on Bankruptcy Proceedings and Liquidation Proceedings.
	<b>Customary kinds of security devices on immoveables</b>
	Real property mortgage and the seceded lien.
	<b>Customary kinds of security devices on moveables</b>
	Mortgage on moveables, pledge on moveables, floating charge and security deposit in the form of money or securities.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Moratorium in case of reorganisation.
	<b>Duties of the insolvency administrator</b>
	To provide information, authorise any kind of business activity in case of reorganisation and act as the executive officer of the business organisation under liquidation.
	<b>Set-off and post-filing credit</b>
	As a general rule under the duration of the stay of payment set-off may not be applied against the debtor. In case of reorganisation, the debtor shall be allowed to undertake any new commitment subject to the consent of the administrator. In case of liquidation, the head of the debtor economic operator shall be restricted from entering into any contract considered to be in excess of the scope of normal operations.
	<b>Creditor claims and appeals</b>
	No claim will be registered in the event of the creditor's failure to do so in due time. The registration of claims is subject to a registration fee payable by the creditor. Creditors may appeal the decisions of the administrator regarding the approval or the ranking of their claims.
	<b>Priority claims</b>
	Certain claims such as secured claims or debts owed to social security funds enjoy priority status.
<b>Major kinds of voidable transactions</b>	
Contracts if intended to conceal the debtors' assets or to defraud any one creditor or the creditors, contracts if intended to transfer the debtors assets without any compensation or to undertake any commitment for the encumbrance of any part of the debtors assets, or if the stipulated consideration constitutes unreasonable and extensive benefits to a third party, contracts if intended to give preference and privileges to any one creditor or to provide financial collateral to a creditor that does not have any, in certain cases may be considered voidable.	
<b>Operating and financing during reorganisations</b>	
With the authorisation of the bankruptcy administrator.	
<b>International cooperation and communication</b>	
The EU Insolvency Regulation applies.	
<b>Liabilities of directors and officers</b>	
Creditors or the liquidator may bring action during the liquidation proceedings to establish that the former executives of the economic operator failed to properly represent the interests of creditors. Any creditor may bring action for the court to establish the liability of the debtor's former executive and hence to order this executive to satisfy the debtor's claim to the extent of its claims not yet satisfied.	
<b>Pending legislation</b>	
None.	

<b>INDIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Companies Act, 1956. Companies Act, 2013. Sick Industrial Companies (Special Provisions) Act, 1985. RBI's Corporate Debt Restructuring mechanism. RBI's Scheme for Sustainable Structuring of Stressed Assets.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages.
	<b>Customary kinds of security devices on moveables</b>
	Fixed charge. Floating charge. Hypothecation. Pledge. Lien.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	No suit or legal proceeding allowed without Court approval.
	<b>Duties of the insolvency administrator</b>
	Preparing report based on statement of affairs. Presenting account of liquidation at general meetings. Keeping records of occurrences at general meetings.
	<b>Set-off and post-filing credit</b>
	Set-off: <ul style="list-style-type: none"> <li>• claims to be mutual, commensurable, ascertainable, liquidated.</li> <li>• rights fixed as on date of commencement of winding-up - sums due post such date not allowed to be set-off.</li> </ul> Post - filing credit <ul style="list-style-type: none"> <li>• liquidator may raise interim finance, on security of company's assets.</li> <li>• scheme for rehabilitation may provide for financial assistance from government, banks or public financial institutions, etc.</li> <li>• CDR: additional finance obtainable subject to conditions.</li> </ul>
	<b>Creditor claims and appeals</b>
	Appeals from Court - same as in ordinary course. Appeals from BIFR - Appellate Authority for Industrial and Financial Reconstruction.
	<b>Priority claims</b>
	Debts due to secured creditors and workmen's dues. Costs of winding-up. Preferential payments (including government and statutory dues). Unsecured creditors. Shareholders.
	<b>Major kinds of voidable transactions</b>
	Onerous property. Fraudulent preference (which is void).
	<b>Operating and financing during reorganisations</b>
	See post-filing credit.
	<b>International cooperation and communication</b>
	Execution of foreign decrees under the Code of Civil Procedure, 1908.
<b>Liabilities of directors and officers</b>	
Imprisonment and/or fine for: <ul style="list-style-type: none"> <li>• default in preparing statement of affairs;</li> <li>• falsification of books or maintenance of improper accounts;</li> <li>• fraudulent conduct of business;</li> <li>• inducement of another to give credit under false pretence or fraud;</li> <li>• transfer of company's property to defraud creditors; and</li> <li>• concealment of property from creditors.</li> </ul>	
<b>Pending legislation</b>	
Insolvency and Bankruptcy Code, 2016.	

<b>INDONESIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Bankruptcy Law and the Company Law.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage (for fixed assets) and hypothec (for registered vessels).
	<b>Customary kinds of security devices on moveables</b>
	Pledge and fiducia transfer of ownership and fiduciary assignment of rights.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	90 days in bankruptcy; and 270 days in suspension of payments.
	<b>Duties of the insolvency administrator</b>
	The receiver in bankruptcy proceedings must manage the bankruptcy estate.
	<b>Set-off and post-filing credit</b>
	The administrator in suspension of payments proceedings, together with the debtor (individual) or the board of directors of the director (company) manage the assets of the debtor.
	<b>Creditor claims and appeals</b>
	A claim must be submitted to the receiver (in bankruptcy proceedings) or administrator (in suspension of payments proceedings). If the claim is denied, an appeal can be submitted to the supervisory judge.
	<b>Priority claims</b>
	Tax claims. Post-bankruptcy creditors (who have claims on the bankruptcy estate) are entitled to receive the following payments in full: <ul style="list-style-type: none"> <li>• salary of the Receiver;</li> <li>• costs in the liquidation of the bankruptcy estate (appraiser's fee, accountant's fee, etc.);</li> <li>• post-bankruptcy financing;</li> <li>• lease of the bankrupt's house or offices; and</li> <li>• wages of the employees of the bankrupt company.</li> </ul> Secured creditors. Unsecured creditors: Specific statutorily preferred creditors whose preference relates only to specific assets. Specific statutory preferred creditors prevail over general statutory priority rights. General statutory priority rights. Non-preferred unsecured creditors.
	<b>Major kinds of voidable transactions</b>
Preferential transfer.	
<b>Operating and financing during reorganisations</b>	
In bankruptcy proceedings financing is allowed, but if new security is required there must be the approval of the supervisory judge. In suspension of payments proceedings it is allowed.	
<b>International cooperation and communication</b>	
There is the principle of territoriality. A bankruptcy procedure initiated in another jurisdiction has, in principle, no effect in Indonesia.	
<b>Liabilities of directors and officers</b>	
Directors are liable if the bankruptcy is caused by their fault.	
<b>Pending legislation</b>	
No pending legislation.	

<b>ISLE OF MAN</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Companies Act 1931. Companies Act 2006. The Companies (Winding Up) Rules 1934.
	<b>Customary kinds of security devices on immovables</b>
	Mortgages. Fixed and Floating Charges. Debentures.
	<b>Customary kinds of security devices on moveables</b>
	Liens. Pledges. Debentures. Title retention.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Winding up order made by court. Provisional liquidator appointed.
	<b>Duties of the insolvency administrator</b>
	N/A.
	<b>Set-off and post-filing credit</b>
	Set off is applicable in both insolvencies and reorganisations.
	<b>Creditor claims and appeals</b>
	Creditors must submit proofs of debt to the liquidator. Appeals against liquidator's decision to the court.
	<b>Priority claims</b>
	Liquidator's costs. Debts to the Crown. Employee entitlements. Unpaid pension contributions. Secured creditors. Unsecured creditors.
	<b>Major kinds of voidable transactions</b>
	Fraudulent preference.
	<b>Operating and financing during reorganisations</b>
	Companies can carry on operating. Directors to manage the business appropriately.
<b>International cooperation and communication</b>	
Courts are keen to assist foreign jurisdictions. UNCITRAL not adopted.	
<b>Liabilities of directors and officers</b>	
Fraudulent trading. Misfeasance.	
<b>Pending legislation</b>	
None.	

<b>ITALY</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Civil Code. The Insolvency Act 1942. The Legislative Decree governing the extraordinary administration. Provisions set out by Law Decree No. 83/2012 (converted into Law No. 134/2012), which introduced important amendments to the insolvency proceedings (the Development Decree). The Law governing the extraordinary administration of large enterprises. The Legislative Decrees implementing the bank Recovery and Resolution Directive. Several provisions of the Banking Law that apply where banks and financial intermediaries are subject to compulsory administrative liquidation. The EU Insolvency Regulation that affects cross-border insolvencies.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages
	<b>Customary kinds of security devices on moveables</b>
	Pledges over property, bank accounts and shares. Non-possessory pledge over equipment used in business activities.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Involuntary liquidation: Foreclosure proceedings commenced by creditors are suspended. Voluntary and involuntary reorganisations: Foreclosure proceedings commenced by creditors are suspended.
	<b>Duties of the insolvency administrator</b>
	Insolvency: Articles 31 et seq of the Insolvency Act set out the duties of the insolvency administrator, who, inter alia, has to notify the creditors of the insolvency order and has to notify those creditors whose claims have been partially admitted or rejected. Reorganisation procedures: Article 165 of the Insolvency Act, article 15 of Law No. 270/1999 and article 3 of Law No. 39/2004 set out the duties of the commissioner, who, among other things, will supervise the day-to-day running of the entity.
	<b>Set-off and post-filing credit</b>
	Article 56 of the Insolvency Act provides for a particular form of legal set-off within bankruptcy proceedings. If it takes place prior to the commencement of bankruptcy it cannot be revoked or avoided.
	<b>Creditor claims and appeals</b>
	Claims normally to be lodged within two months after the declaration of insolvency is made. Outcome of hearing of all the claims may be challenged by any creditors whose claims have not been recognised or have been partially recognised within 30 days.
	<b>Priority claims</b>
	These rank ahead of secured claims: <ul style="list-style-type: none"> <li>• preferential claims (general or special) over moveable property;</li> <li>• preferential claims (general or special) over immovable property.</li> </ul>
	<b>Major kinds of voidable transactions</b>
The relevant rules are set out in Articles 64-70 of the Insolvency Act. Any gratuitous transaction that was completed two years prior to the insolvency order may be set aside. The transactions executed and payments made by the insolvent debtor declared bankrupt during a certain 'suspect period' may be subject to a clawback action. Finally, Article 2901 of the Italian Civil code provides that some acts of disposal of the bankrupt's assets may be declared ineffective against the relevant creditor, when the following conditions are met: 1) the debtor knew the prejudice that the act would cause to the interests of the creditor or, in case of acts done before the origination of the credit, the act was intentionally pre-ordained to adversely affect the fulfilment of the obligation; 2) for acts for consideration, the third party was aware of the prejudice and, in case of acts done before the origination of the credit, he or she intentionally participated in the debtor's plan.	
<b>Operating and financing during reorganisations</b>	
Compositions and judicial moratoria: trading allowed only to the extent necessary to complete particular transactions. Extraordinary administration and extraordinary administration of large enterprises: ministerial decree may allow the company to continue its business.	
<b>International cooperation and communication</b>	
There has been little use of the instruments of cooperation envisaged by Regulation No. 1346/2000. Italian operators in the sector maintain that simpler, more informal types of contact and exchanges of information are needed. As regard to the recognition of judgments declaring insolvency issued in another member state, Italian case law reveals a generalised application of such principle.	
<b>Liabilities of directors and officers</b>	
May be liable to the company, the company's creditors and to third parties under rules established by the Civil Code. In addition, under the Insolvency Act, directors and de facto officers may be charged with criminal liability for fraudulent bankruptcy, simple bankruptcy and illicit borrowing.	
<b>Pending legislation</b>	
Legislation based on the UNCITRAL Model Law on Cross-Border Insolvency has not yet been adopted.	

<b>JAPAN</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Liquidation-type procedures: <ul style="list-style-type: none"> <li>• Bankruptcy Law – natural and legal persons; and</li> <li>• Companies Act (special liquidations) – joint-stock corporations.</li> </ul> Reorganisation-type procedures: <ul style="list-style-type: none"> <li>• Civil Rehabilitation Law – natural and legal persons; and</li> <li>• Corporate Reorganisation Law – joint-stock corporations.</li> </ul>
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage – debtor retains possession. Pledge – creditor possesses collateral. Security by way of transfer – debtor maintains possession for creditor. Preferential right – creditors secured by operation of law.
	<b>Customary kinds of security devices on moveables</b>
	Pledge – creditor possesses collateral. Possessory lien – creditor possesses collateral. Security by way of transfer – debtor maintains possession for creditor. Preferential right – creditors secured by operation of law. Reservation of ownership – seller retains ownership.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	A court order for commencement of bankruptcy or reorganisation stays civil suits and compulsory executions or other executions of creditor’s rights, except most foreclosures by secured creditors (under the corporate reorganisation procedure, however, foreclosures by secured creditors are also prohibited). Under a certain liquidation (special liquidation): compulsory executions or other executions of unsecured rights will be stayed; and the court may take measures to preserve the assets of the debtor company or other measures such as prohibition of updating the shareholders register.
	<b>Duties of the insolvency administrator</b>
	Draft a rehabilitation or reorganisation plan and submit it to the court (under the civil rehabilitation and the corporate reorganisation procedure). Sell assets of the debtor and make distribution to the creditors (under the bankruptcy procedure). Represent the debtor when a lawsuit is filed regarding the assets of the debtor.
	<b>Set-off and post-filing credit</b>
	Subject to certain exceptions, if a creditor owes a debt to a debtor at the time of the commencement of the relevant insolvency procedure, the creditor may set off that debt against its claim owed by the debtor until the completion of the procedure (bankruptcy procedure and special liquidation procedure) or the expiration of the claim filing period (in a civil rehabilitation procedure and corporate reorganisation procedure). A debtor and a trustee-in-bankruptcy or an administrator, on behalf of the debtor, can borrow money with the approval of the court (which may not be required in a civil rehabilitation procedure and a corporate reorganisation procedure).
	<b>Creditor claims and appeals</b>
	Except in special liquidation procedures the court decides and publicly announces the period for filing claims, during which creditors must file their claims against the debtor with the court to be able to participate in the proceedings. If a creditor’s claim is disputed by the debtor, the trustee-in-bankruptcy, the administrator or any other creditor, the creditor may initiate legal action against the person objecting to the claim. If no objection has arisen with respect to a claim at a creditors’ meeting or within the claim examination period, the amount and priority of the claim will be finalised. In relation to a special liquidation procedure, creditors must submit their claims to a liquidator but there is no specific provision regarding how to submit a claim, which claims will be disallowed or what action the creditor should take to challenge a disallowance.
	<b>Priority claims</b>
	Generally, secured creditors have first priority, but, in some reorganisations ‘common benefit’ claims (taxes, wages, expenses, etc) have priority over secured creditors.
	<b>Major kinds of voidable transactions</b>
	Any acts of the debtor (excluding the creating of securities or dissolving of debts) that were taken with the knowledge that such action would jeopardise the interests of the creditors. Any acts of the debtor (excluding the creating of securities or dissolving of debts) that would jeopardise the interests of the creditors conducted after suspension of payments or the filing of a petition for commencement of bankruptcy procedures. Dispositions of debtor’s assets in exchange for cash that may actually enable the debtor to jeopardise the interests of the creditors by hiding cash or disposing cash for free. Any acts of the debtor (limited to creating securities or dissolving debts) conducted after the debtor became unable to pay its debts or after the filing for a petition for the commencement of insolvency procedures. Any acts of the debtor (limited to creating securities or dissolving debts) that are not included in the scope of the debtor’s obligation in terms of the act itself or the time of the performance of the act, that were conducted within 30 days before the debtor became unable to pay its debts.
	<b>Operating and financing during reorganisations</b>
Generally, the administrator operates business. The debtor may operate business under the civil rehabilitation procedure. Court approval may be required for the disposition and assumption of any assets; borrowing; filing a lawsuit; and any other acts specified by the court.	
<b>International cooperation and communication</b>	
Under the ARAFIP, a foreign administrator may file a request to the Japanese court to recognise the foreign proceedings and take necessary measures including the foreclosure of assets and appointment of a domestic administrator in Japan. The Bankruptcy Law, the Civil Rehabilitation Law and the Corporate Reorganisation Law also address the cooperation between domestic administrators and foreign administrators in cross-border insolvency and restructurings.	
<b>Liabilities of directors and officers</b>	
If a corporation causes damage to a third party because of the wilful misconduct or gross negligence of its director, that director will be liable to the third party. Also if a director or officer of a debtor enters into a transaction with a third party and does not inform that third party that the debtor is insolvent or is likely to become insolvent and the third party suffers damage as a result of a subsequent insolvency, the director or officer can be punished on the basis that he or she has committed fraud under the Criminal Code. Furthermore, in bankruptcy, civil rehabilitation and corporate reorganisation procedures, certain actions of a debtor’s director that jeopardise the interests of the debtor’s creditors (eg, hiding or destroying any assets of the debtor or amending, hiding or destroying financial records of the debtor) will be punished.	
<b>Pending legislation</b>	
None.	

<b>LUXEMBOURG</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Articles 437 ff of the Commercial Code, controlled management under the Grand-Ducal Decree dated 24 May 1935, reprieve from payments articles 593 ff of the Commercial Code, and composition with creditors, articles 508 to 527 of the Commercial Code.
	<b>Customary kinds of security devices on immoveables</b>
	Mainly mortgages.
	<b>Customary kinds of security devices on moveables</b>
	For holding companies, mainly pledges regulated by Financial Collateral Law.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	As from the judgment there is a stay of proceedings except for secured creditors benefiting from the Financial Collateral Law.
	<b>Duties of the insolvency administrator</b>
	The insolvency administrator acts on behalf of the company and the creditors. He or she shall act cautiously, diligently and in full independence.
	<b>Set-off and post-filing credit</b>
	Legal set-off possible. Set-off agreements under the Financial Collateral Law are opposable to insolvency administrators. Post-filing credit is possible (subject to prior approval of either the delegated judge or the commissioners appointed by the court) in case of controlled management.
	<b>Creditor claims and appeals</b>
	Creditor claims (and evidence of claim) to be submitted within a maximum of 20 days from the bankruptcy judgment but deadline is not compulsory. If the insolvency administrator disputes the claim, the court decides. Appeal of such decision is possible.
	<b>Priority claims</b>
Secured creditors (collateral or mortgage) have priority claims. Some other creditors have general priority claims: <ul style="list-style-type: none"> <li>• employees;</li> <li>• social security (for both employee's and employer's contribution);</li> <li>• taxes (direct and indirect); and</li> <li>• landlord, pledgor not under the Financial Collateral Law and vendor's privilege.</li> </ul>	
<b>Major kinds of voidable transactions</b>	
<ul style="list-style-type: none"> <li>• Disposition of assets without consideration of material adequacy;</li> <li>• payments of debts, which had not fallen due, whether the payment was in cash or by way of assignment, sale, set-off, or by any other means;</li> <li>• payments of debts, which had fallen due, by any means other than in cash or by bills of exchange; and</li> <li>• mortgages or pledges granted to secure pre-existing debts.</li> </ul>	
<b>Operating and financing during reorganisations</b>	
Agreements will continue, prior approval of certain transactions required from either the delegated judge or the commissioners appointed. Financing is permitted but subject to prior approval from either the delegated judge or the commissioners appointed.	
<b>International cooperation and communication</b>	
Admitted in cross-border cases.	
<b>Liabilities of directors and officers</b>	
Directors and officers are usually not liable for the company's debts but they might be held liable in certain circumstances (late filing of bankruptcy, for example).	
<b>Pending legislation</b>	
Bill of Law No. 6539 under review.	

<b>MALAYSIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Companies Act 1965 provides for winding up and reorganisations through schemes of arrangements.
	<b>Customary kinds of security devices on immoveables</b>
	Registered fixed and floating charges and liens.
	<b>Customary kinds of security devices on moveables</b>
	Registered fixed and floating charges.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	There is no automatic moratorium in a scheme of arrangement. A moratorium order called a restraining order will have to be applied for from the court. Upon the making of a winding up order, there is a stay of all legal proceedings against the company unless leave of the court is obtained.
	<b>Duties of the insolvency administrator</b>
	Primarily, to realise the assets and to then distribute the assets in the order of statutory priority before paying out to the unsecured creditors.
	<b>Set-off and post-filing credit</b>
	Both are allowed for.
	<b>Creditor claims and appeals</b>
	Unsecured creditors would make their claims by filing a proof of debt. The decision in relation to the admission or rejection of the proof of debt can be appealed to the court.
	<b>Priority claims</b>
	There are a list of priority claims. Generally, the fees and expenses of winding up, followed by employee-related claims, and federal taxes.
	<b>Major kinds of voidable transactions</b>
There are various transactions liable to be made voidable, from a period ranging from six months to five years before the commencement of winding up.	
<b>Operating and financing during reorganisations</b>	
With no restraining order in place, the company would continue operate as usual. With a restraining order, there cannot be any disposition of property outside the ordinary course of business.	
<b>International cooperation and communication</b>	
Malaysia is not a party to any treaty on cross-border insolvency or reorganisation. The Malaysian courts do not have cross-border insolvency protocols.	
<b>Liabilities of directors and officers</b>	
Directors and officers can be made personally liable for the debts of the wound-up company, if they have been guilty of insolvent trading or fraudulent trading.	
<b>Pending legislation</b>	
The Companies Act 2016 has been gazetted but not brought into force yet. This new legislation will revamp the insolvency and reorganisation laws, and introduce two new corporate rescue mechanisms.	

<b>MEXICO</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Bankruptcy Law (LCM).
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage, industrial mortgage and guarantee trust.
	<b>Customary kinds of security devices on moveables</b>
	Ordinary pledge, pledge with debtor's holding pledge possession, bonding guarantee (surety bond) guarantee trust, aval (joint and several personal guarantee on a negotiable instrument), joint and several obligation and personal guarantee.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Executions, attachments and seizures are stayed. Pre-filing legal actions and post-filing legal actions against the debtor are not joined and shall be prosecuted until the final judgment when they shall be recognised in amount and preference. Enforcement of legal actions against the debtor or estate assets does not stay reorganisation or liquidation. In general, reorganisation and liquidation proceedings may not be stayed.
	<b>Duties of the insolvency administrator</b>
	In reorganisation, while a debtor is in possession, a conciliator is in charge of creating and formalising a plan; determining allowed and disallowed claims for court approval; and overseeing the debtor in possession performance. In liquidation, trustee is in possession; pursue process for allowed or disallowed claims for court approval and liquidates estate assets and make payment of dividends. The insolvency administrator is in charge of collecting and selling the assets for creditors' payment.
	<b>Set-off and post-filing credit</b>
	Set-off is partially allowed. In conciliation (reorganisation) secured or unsecured loans may be executed upon the conciliator's decision and in bankruptcy (liquidation) by the trustee's decision, with the previous opinion of administrators and court approval.
	<b>Creditor claims and appeals</b>
	All claims should be filed within 20 working days as of the publication of the insolvency adjudication. Claims may be filed thereafter but no later than the time allowed for the appeal against recognition, rankings and preferred claims. Creditors may appeal this judgment. The following may be appealed: judgment of declaration of general insolvency proceedings (insolvency adjudication), reorganisation plan approval, bankruptcy adjudication and general insolvency proceedings termination. All other insolvency court orders may be challenged, by revocation remedy, and are decided by the same insolvency court.
	<b>Priority claims</b>
	Post-filing financing, estate administration costs and contracts for the ordinary management and administration of the estate as an ongoing concern, labour credits, tax credits, and secured claims have priority against estate assets.
	<b>Major kinds of voidable transactions</b>
Gratuitous acts (donations), fraudulent asset conveyances, encumbrances, liens, preferences and payments executed as of the suspect period.	
<b>Operating and financing during reorganisations</b>	
All ordinary business acts are allowed, including contracting, financing, collateralisation, substitutions of collateral and transfers of assets not necessary for ordinary business. Other acts outside ordinary business need court approval.	
<b>International cooperation and communication</b>	
LCM incorporates generally in Chapter 12 of the UNCITRAL Model Law on Cross Border Insolvency. Mexican courts welcome insolvency cooperation and court-to-court communication as well as recognition and enforcement of foreign insolvency proceedings. If a debtor has an establishment in Mexico, for recognition of foreign insolvency proceedings a full general insolvency proceedings must be pursued. If a debtor lacks an establishment in Mexico, recognition and enforcement of foreign insolvency proceedings may be granted after a summary proceeding.	
<b>Liabilities of directors and officers</b>	
Tax, labour, civil and criminal personal liability for the unlawful management and administration of the enterprise. Any new administration must report any wrongdoing uncovered, otherwise it will be liable.	
<b>Pending legislation</b>	
Substantial amendments to the LCM came into force on 11 January 2014.	

<b>NETHERLANDS</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Bankruptcy Act. There are special provisions in the Financial Supervision Act for financial institutions.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages.
	<b>Customary kinds of security devices on moveables</b>
	Pledges.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	In bankruptcy: stay of proceedings with respect to claims against the bankrupt. No enforcement of unsecured claims. In suspension of payment: enforcement measures of unsecured non-preferential claims can be stopped.
	<b>Duties of the insolvency administrator</b>
	In bankruptcy: to manage and liquidate the assets. In suspension of payments: to manage the assets jointly with the managing board. In a pre-pack: an advisory role in which he explores and prepares restructuring measures together with the debtor and the most important (secured) creditors.
	<b>Set-off and post-filing credit</b>
	Both in bankruptcy and 'suspension of payments' but not automatic. There is no legal basis for post-filing credit: in practice a post filing credit is granted and treated as a super senior estate claim.
	<b>Creditor claims and appeals</b>
	In bankruptcy: claims are submitted to the trustee and can be disputed by the trustee and the other creditors in a claims allowance meeting. In 'suspension of payments' creditors will have to file their claims if a reorganisation plan is submitted by the debtor.
	<b>Priority claims</b>
	The most important priorities: <ul style="list-style-type: none"> <li>• claims arising after the commencement of the insolvency proceedings;</li> <li>• tax claims, security premiums; and</li> <li>• wages and pension claims.</li> </ul>
	<b>Major kinds of voidable transactions</b>
	The trustee in bankruptcy may void transactions for consideration which have been entered into without obligation to do so if the act was detrimental to the creditors and both the debtor and the other party at that time knew or should have known it to be detrimental to the creditors.
	<b>Operating and financing during reorganisations</b>
	Since post-petition debts have priority it may be easier to attain fresh money during the insolvency proceedings. Both in bankruptcy and in a suspension of payment the business may be continued.
<b>International cooperation and communication</b>	
The EU Insolvency Regulation provides an obligation for cooperation and information exchange between liquidators. Cooperation and communication is not dealt with explicitly in the Dutch Bankruptcy Code. In practice, coordination or cooperation does occur and cross-border insolvency agreements (protocols) have been used.	
<b>Liabilities of directors and officers</b>	
Managing directors may be liable to the company in bankruptcy for mismanagement. They may also be liable to the tax authorities, the social security institutions and the pension funds. New legislation has not only introduced the possibility of managing directors being disqualified but has also increased the risk of criminal liability for managing directors.	
<b>Pending legislation</b>	
Various legislative proposals for legislation to amend the Dutch Bankruptcy Act have been published on the Dutch government website for public consultation and/or submitted to the Dutch Lower House for approval. Further, a legislative proposal for the pre-pack procedure is currently awaiting approval by the Dutch Senate (once approved the new pre-pack legislation is expected enter into force sometime in 2017).	

<b>NIGERIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Companies and Allied Matters Act (CAMA) Cap, C20, Laws of the Federation of Nigeria, 2004, Investment and Securities Act 2007 and Securities and Exchange Commission Rules 2013, Banks and other Financial Institutions Act, Cap B3, Laws of the Federation of Nigeria, Cap B3, Laws of the Federation of Nigeria, 2004, Nigerian Deposit Insurance Corporation Act, Cap N 102, Laws of the Federation of Nigeria, 2004, Assets Management Corporation of Nigeria Act, 2010, Bankruptcy & Insolvency (Repeal and Re-enactment) Act 2016 and Bankruptcy Rules.
	<b>Customary kinds of security devices on immoveables</b>
	Legal mortgage and charges by way of debenture in urban areas and pledges and equitable mortgages in rural areas.
	<b>Customary kinds of security devices on moveables</b>
	Charge on the property itself.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	A shareholder, the company or creditor may apply for stay of proceedings and the court if satisfied with the reasons for such application would adjourn the proceedings to a later date.
	<b>Duties of the insolvency administrator</b>
	Defend legal proceedings on behalf of company, carry on business of the company for the benefit of the winding up, appoint professionals to assist him or her in performance of his or her duties, pay any class of creditors and make any compromise or arrangement with the creditors.
	<b>Set-off and post-filing credit</b>
	Whether limited or unlimited company, when all creditors are paid in full, the money due on any account to a contributory may be allowed to him or her by way of set-off against any subsequent call.
	<b>Creditor claims and appeals</b>
	Where a creditor cannot prove his or her claim, it will not be considered in the liquidation order. A creditor may appeal against the liquidation order to the Court of Appeal.
	<b>Priority claims</b>
	Labour-related claims rank equally among themselves. After labour claims are claims of secured creditors.
	<b>Major kinds of voidable transactions</b>
Reorganisation contrary to the provisions of the Companies and Allied Matters Act is null and void. In liquidation, any conveyance or assignment by a company of all its property to trustees for the benefit of all its creditors shall be void.	
<b>Operating and financing during reorganisations</b>	
If the liquidator elects to purchase the shares of any member who dissents to the transfer of shares to a transferee company, the price payable on the member's shares shall be determined by agreement in the case of a private company with no foreign participation. In the case of a public company or private company with foreign participation, the price shall be determined by the Securities and Exchange Commission.	
<b>International cooperation and communication</b>	
Monetary judgments and orders from Commonwealth countries are enforceable in Nigeria under the Reciprocal Enforcement of Foreign Judgments Ordinance, Cap 175, 1958, and leave for enforcement is filed in a High Court in Nigeria within 12 months of the date of the judgment or order. The Bankruptcy & Insolvency (Repeal and Re-enactment) Act provides that where there is a bankruptcy or insolvency, a reorganisation order made against a debtor in a foreign proceeding means that a certified copy of the order is, in the absence of contrary evidence, proof that the debtor is insolvent and appointment of a foreign representative has been made. The Nigerian court would assist foreign representatives as long as it is not inconsistent with the provisions of the Bankruptcy & Insolvency (Repeal and Re-enactment) Act.	
<b>Liabilities of directors and officers</b>	
Where a director before winding up of a company fails to deliver to the liquidator all the company's property and the accurate books in his custody, such a director is guilty of an offence and is liable upon conviction to 12 months' imprisonment.	
<b>Pending legislation</b>	
The Bankruptcy and Insolvency (Repeal and Re-Enactment) Act, 2016 is a welcome development. It provides for corporate and individual insolvency, rehabilitation of insolvent debtors, creates the office of supervisor of insolvency and recognises insolvency orders from foreign jurisdictions and appointment of foreign representatives.	

<b>NORWAY</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Main statutes: The Bankruptcy Act of 8 June 1984 No. 58. The Satisfaction of Claims Act of 8 June 1984 No. 59.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages and execution liens.
	<b>Customary kinds of security devices on moveables</b>
	Pledges, either in each asset or floating charges, and execution liens.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Yes.
	<b>Duties of the insolvency administrator</b>
	Handle all aspects of the proceedings; more or less functions as the chairman of the board and CEO if compared with a limited liability company.
	<b>Set-off and post-filing credit</b>
	Set-offs may be allowed. Post-filing credit is not allowed.
	<b>Creditor claims and appeals</b>
	Claims may usually be filed in the estate throughout the proceedings; there is no preclusive deadline. Claims are subject to a set order of priorities. Claims are tested by the administrator/creditors' committee, and potentially the court. The court's decisions may in general be appealed within one month from passing.
	<b>Priority claims</b>
	Employees' claims for wages rank first in priority, and certain VAT and tax claims rank second in priority. The next class of priority is unsecured claims.
	<b>Major kinds of voidable transactions</b>
Transactions of a certain size within last three months before proceedings were opened, covering old debt, gifts, transactions beneficial to closely related parties.	
<b>Operating and financing during reorganisations</b>	
Operations continue as usual during debt negotiation proceedings. Financing during debt negotiation proceedings is not allowed unless accepted by the administrator/creditors' committee.	
<b>International cooperation and communication</b>	
Little or no cooperation between Norwegian and foreign courts.	
<b>Liabilities of directors and officers</b>	
May potentially be held criminally or financially liable.	
<b>Pending legislation</b>	
Changes in the Bankruptcy Act, providing new legislation on cross-border cases. It is not yet decided when the changes will enter into force.	

<b>PERU</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Law No. 27809.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages and trusts.
	<b>Customary kinds of security devices on moveables</b>
	Pledges and trusts.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Yes. With the publication of the debtor's insolvency in the official gazette (bar date). Available in all insolvency proceedings regulated by the Insolvency Law.
	<b>Duties of the insolvency administrator</b>
	Not specified.
	<b>Set-off and post-filing credit</b>
	Set-off is banned from the bar date and during the avoidance period.
	<b>Creditor claims and appeals</b>
	Creditors must file their proofs of claims before INDECOPI within 30 business days from the bar date. Appeals are available.
	<b>Priority claims</b>
	Labour claims (included pension claims), alimony claims (applicable only when the insolvent is an individual), secured claims (including attachments and seizures), tax claims and non-secured claims.
	<b>Major kinds of voidable transactions</b>
None.	
<b>Operating and financing during reorganisations</b>	
No priority is given by the Insolvency Law.	
<b>International cooperation and communication</b>	
None.	
<b>Liabilities of directors and officers</b>	
Applicable for acts against the law, the bylaws or acts of fraud, gross negligence or those resulting from the abuse of their faculties. Directors are joint and severally liable with the companies before the tax authorities when tax debts are not paid due to manager's gross negligence, fraudulent acts with the intent to cause harm or abuse of powers.	
<b>Pending legislation</b>	
The Insolvency Law was recently amended by means of Legislative Decree No. 1189, which came into force on 20 October 2015.	

<b>ROMANIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Law No. 85/2014 regarding insolvency prevention mechanics and insolvency proceedings.
	<b>Customary kinds of security devices on immoveables</b>
	Immoveable hypothec agreements.
	<b>Customary kinds of security devices on moveables</b>
	Moveable hypothec agreements (on bank accounts, receivables, shares, etc).
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Automatic stay when insolvency proceedings are opened. Exceptions are provided by the Insolvency Law (eg, claims concerning the property rights).
	<b>Duties of the insolvency administrator</b>
	Preparing reports during the insolvency procedure (eg, report on the insolvency causes and responsible persons, monthly activity reports). Verifying receivables and drawing-up receivables table. Deciding on what contracts to keep or terminate. Summoning creditors' meetings. Filing claims for annulment of fraudulent acts concluded by the debtor, filling claims in order to recover receivables.
	<b>Set-off and post-filing credit</b>
	Legal set-off allowed. Set-off under ISDA master agreements not impacted. Post-filing financings benefit from priority.
	<b>Creditor claims and appeals</b>
	Requests for claims admission must be filed after the opening of insolvency. Claims are verified by the judicial receiver. Claims admitted are recorded in the receivables list. Creditors may appeal to the judicial receiver's decision within seven days from publication of the preliminary receivables list.
	<b>Priority claims</b>
	Taxes and other expenses related to the sale of assets and to the insolvency proceedings. Conservation expenses, after the opening of the insolvency. Claims of creditors benefiting from preference rights (such as secured creditors) that came into existence during the insolvency proceedings. Other claims enjoying preference causes.
	<b>Major kinds of voidable transactions</b>
	Free transfer acts. Securing an unsecured debt. Early prepayments.
	<b>Operating and financing during reorganisations</b>
	The debtor can carry on business during reorganisation with or under the supervision of the judicial receiver and of the insolvency judge, in accordance with the confirmed reorganisation plan. Financing arrangements granted to the debtor for the purpose of conducting its usual business, if approved by the creditors, benefit from priority at repayment.
<b>International cooperation and communication</b>	
Specific procedures for recognition of foreign insolvency proceedings and for cooperation between domestic and foreign courts and foreign insolvency administrators. Courts may refuse to recognise a foreign insolvency procedure or a foreign judgment in case of fraud and breach of Romanian private international law public order provisions.	
<b>Liabilities of directors and officers</b>	
As soon as insolvency has become manifest, directors are obliged to file an insolvency request with the competent court. Liability for insolvency of the debtor. Criminal liability.	
<b>Pending legislation</b>	
Not applicable.	

<b>RUSSIA</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Civil Code; Federal Law on Insolvency (Bankruptcy); Federal Law on Financial Restoration of Agricultural Commodity Produces; Federal Law No. 29-FZ on Enforcement Proceedings.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage (subject to state registration).
	<b>Customary kinds of security devices on moveables</b>
	Pledge (may be registered by a notary in the register of pledge notices at the discretion of pledgor or pledgee).
	<b>Stays of proceedings in reorganisations/liquidations</b>
	In general, upon commencement of bankruptcy procedure, no claims against the debtor's assets may be enforced. Ordinary corporate reorganisations/liquidations of companies do not have the said effects.
	<b>Duties of the insolvency administrator</b>
	Supervision: to identify creditors, prepare a report on the debtor's financial status and convene the first creditors' meeting. Financial restoration: to monitor performance of the debtor's obligations in accordance with a plan and payment schedule. External administration: to prepare a reorganisation plan, to deal with the debtor's assets to restore its solvency. Bankruptcy proceedings: to evaluate all assets of the debtor and sell them separately or as an entire business to satisfy the creditors' claims.
	<b>Set-off and post-filing credit</b>
	Generally, set-off is permitted provided that it does not affect the priority of claim satisfaction and does not entail preferential claim satisfaction. The debtor is not prevented from obtaining loans or credits. Claims that arise from such loans and credits outrank all other claims.
	<b>Creditor claims and appeals</b>
	Creditors are allowed to submit their claims at any time during the bankruptcy proceedings. As a general rule, claims must be confirmed by a judgment or an arbitral award (no judgement or arbitral award is required for claims of credit organisations and claims in relation to compulsory payments).
	<b>Priority claims</b>
	Generally as follows: personal injury and some related claims; employee's and copyright-fees claims; and all other claims including (claims by secured creditors that, however, may in some cases prevail over first and second-ranking creditors). Distributions to creditors may be made at any stage of the bankruptcy procedure.
	<b>Major kinds of voidable transactions</b>
	In general, any transactions concluded by the debtor in violation of the Federal Law on Insolvency (Bankruptcy) may be set aside. Major kinds of voidable transactions are: transactions concluded within a particular period that negatively affected the debtor's financial position or the economic interests of creditors (other than those who have entered into such voidable transactions).
	<b>Operating and financing during reorganisations</b>
	During the supervision stage or financial restoration, an insolvency office holder supervises the debtor's management and limits its authority. In external administration or bankruptcy proceedings an insolvency office holder replaces the debtor's management. Any shareholder of an insolvent company or any third party can, at any time before the end of bankruptcy proceedings, offer to pay all of the company's debts to prevent its ultimate liquidation.
<b>International cooperation and communication</b>	
Russian bankruptcy legislation does not provide any specific rules in respect of cross-border cooperation between domestic and foreign courts and domestic and foreign insolvency administrators in cross-border insolvencies and restructurings. Foreign court decisions on insolvency (bankruptcy) are recognised in Russia based on international treaties and the principle of reciprocity.	
<b>Liabilities of directors and officers</b>	
Criminal and administrative liability: providing misleading information in financial and accounting documents of an organisation with the intention to suppress the signs of insolvency, misbehaviour in the course of bankruptcy, fictitious or intentional bankruptcy. Civil liability for the company's debts in case of causing the company's bankruptcy as a debtor controlling person or failure to file a bankruptcy petition when necessary; and for losses caused by breach of duty to act in the interests of the company, reasonably and in good faith.	
<b>Pending legislation</b>	
No significant pending legislation.	

<b>SINGAPORE</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Companies Act.
	<b>Customary kinds of security devices on immoveables</b>
	Legal mortgages and equitable mortgages.
	<b>Customary kinds of security devices on moveables</b>
	Fixed and floating charges.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Winding up: no automatic stay of legal proceedings against the company after a winding up application is presented. Automatic stay of proceedings against the company upon the making of a winding-up order or the appointment of a provisional liquidator, unless the court gives leave for the proceedings to continue. Judicial management: automatic stay of all proceedings upon the application for the Judicial Management Order. Court may grant leave based on balance of interests of applicant and other creditors. Schemes of arrangement: no automatic stay of proceedings, an application may be made to court for an order that proceedings pending against the company be stayed. The application must be bona fide and be of sufficient particularity.
	<b>Duties of the insolvency administrator</b>
	<ul style="list-style-type: none"> <li>• submit preliminary report to official receiver as to capital, assets and liabilities;</li> <li>• every six months, lodge account of receipts and payments, and statement of position of the winding up;</li> <li>• call for, receive and assess proofs of debt; and</li> <li>• liquidate assets for distribution to creditors.</li> </ul>
	<b>Set-off and post-filing credit</b>
	Winding up: set-off of mutual debts, liabilities and dealings. Judicial management: contractual set-off permitted.
	<b>Creditor claims and appeals</b>
	Proofs of debt to be filed three months after winding-up order. Notice for filing of proofs to be made at least 14 days in advance. All claims including present, future, certain, contingent, ascertained, or unliquidated may be presented. Appeals may be made to the court.
	<b>Priority claims</b>
	In the following order of priority: <ul style="list-style-type: none"> <li>• costs and expenses of the winding up;</li> <li>• wages and salaries of employees up to a maximum of five months' salary or S\$12,500 (whichever is less);</li> <li>• retrenchment benefits and ex gratia payments under the Act up to a maximum of S\$12,500;</li> <li>• compensation to an employee for injuries suffered in the course of employment under the Work Injury Compensation Act;</li> <li>• remuneration in respect of holiday leave;</li> <li>• taxes; and</li> <li>• gratuity and retrenchment benefits under the Employment Act.</li> </ul>
	<b>Major kinds of voidable transactions</b>
	Unfair preferences given to an associate occurring within two years before the presentation of a winding-up application. Transactions at an undervalue occurring within five years before the presentation of a winding-up application. A floating charge on the undertaking or property of a company created within six months of the commencement of the winding up except to the amount of any cash paid to the company at the time of or subsequently to the creation and in consideration of the charge together with interest on that amount at the rate of 5 per cent per annum unless the company is solvent immediately after the creation of the charge.
	<b>Operating and financing during reorganisations</b>
	Out of the assets of the company.
<b>International cooperation and communication</b>	
Singapore is not a party to any international treaties or protocols pertaining to cross-border reorganisations and rescues. Assistance for foreign winding-up proceedings will depend on the circumstances of the case. When a foreign company goes into liquidation in its place of incorporation or origin, it may be concurrently wound up in Singapore and a liquidator for Singapore will be appointed by the court. He may only recover and realise the assets of the foreign company in Singapore and must pay the net amount recovered and realised to the foreign liquidator after paying any debts and satisfying any liabilities incurred in Singapore by the foreign company.	
<b>Liabilities of directors and officers</b>	
May be held personally liable if breach of directors' fiduciary duties to the company, wrongful trading, and fraudulent trading or misfeasance.	
<b>Pending legislation</b>	
The Insolvency Law Review Committee has presented its report on the omnibus Insolvency Act and public feedback has been obtained.	

<b>SPAIN</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The main regulation of insolvency proceedings is the Insolvency Law, enacted on 9 July 2003, which came into force on 1 September 2004 and that has been subject to several amendments, the last being in October 2015.
	<b>Customary kinds of security devices on immovables</b>
	The principal security device on immovable property is the mortgage. Mortgages must be granted by public deed and be registered in the Land Registry. No security enforceable against third parties is created until the mortgage registration has been completed.
	<b>Customary kinds of security devices on moveables</b>
	The principal security device on moveable property is the possessory pledge. To be enforceable against third parties pledges must be generally granted in a public document and possession over the pledged asset must be transferred either to the pledgee or a depositary.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Declarative proceedings pending at the time of the insolvency declaration will continue but may be consolidated into the insolvency proceedings. New declarative proceedings can be initiated but must be filed with the insolvency court. Unsecured claims for the attachment of assets pending at the time of the insolvency declaration can continue if the assets attached are not required to continue running the business. No new unsecured claims for the attachment of assets can be enforced during the insolvency proceedings. Security over the assets that are used in the debtor's business cannot be initiated until a settlement agreement that does not affect the security/secured claim is approved or a year passes following the insolvency declaration without the liquidation phase being opened. As an exception, this is not applicable to secured claims related to certain financial collateral.
	<b>Duties of the insolvency administrator</b>
	The insolvency receiver's duties may range from mere supervision of the debtor to administration of the debtor's assets and activities. Whether directors are entirely released from their duties or continue in office under the supervision of the receiver will be at the court's discretion in view of the particular circumstances of the case. There is a preference for releasing the directors if the insolvency filing is made by a creditor. The relevant regime and specific insolvency receivers' duties will be decided by the court case by case. See questions 9 and 13.
	<b>Set-off and post-filing credit</b>
	In general, set-off is not permitted in an insolvency proceeding unless the requirements for set-off have been met prior to the insolvency declaration. As an exception to the general regime: set-off provisions complying with the requirements set out in Spanish Royal Decree-Law 5/2005 (which implements EU Directive 2002/47 on financial collateral) will be enforceable in an insolvency scenario; set-off is allowed if the non-Spanish law governing the reciprocal claim allows such set-off in insolvency proceedings. The Insolvency Act does not expressly regulate the debtor's right to obtain secured or unsecured loans but provides that during the insolvency proceedings it is possible to resume loan agreements that have been accelerated in the three months before the insolvency declaration.
	<b>Creditor claims and appeals</b>
	Any claim against the debtor must be filed with the court dealing with the insolvency proceedings. Appeals may be available, under certain circumstances, before the relevant court of appeals.
	<b>Priority claims</b>
	The insolvency debts are classified as follows. Debts of the insolvency estate - These include, among others, debts that originated within the insolvency proceedings (eg, judicial expenses, loan agreements that are rehabilitated by the court, 50 per cent of the fresh money granted within the framework of a refinancing agreement which satisfies some conditions), debts that originated after the insolvency declaration (eg, debts arising from the continuation of the business) and salary claims for the 30 days immediately preceding the declaration of insolvency. Insolvency debts - These debts are classified as: specially privileged debts (among others, debts secured by mortgages or pledges, rental payments arising from lease agreements and instalments arising from hire-purchase agreements); generally privileged debts (among others, salaries and severance payments up to certain limits, certain taxes, credits arising from tort liability, 50 per cent of the fresh money granted within the framework of a refinancing agreement which satisfies some conditions and 50 per cent of the debt of the creditor who applied for the insolvency are classified as generally privileged debts); ordinary debts; or subordinate debts. Debts of the insolvency estate will be paid out of the debtor's assets (other than those assets attached to specially privileged debts) with preference to any other debts. Secured debts are generally paid with the proceeds of the enforcement of the security. Generally privileged debts will be paid by segregating from the debtor's estate those assets covering the aggregate amount of such credits.
<b>Major kinds of voidable transactions</b>	
Acts and contracts entered into by the debtor in the two years before the insolvency declaration may be rescinded by the court on the basis that these acts or contracts are harmful to the insolvency estate. Certain acts and contracts are presumed by law to be harmful to the insolvency estate, without any possibility for the parties to file evidence against this presumption. This is the case for gifts and early payments of unmatured debt. The law also presumes (although admitting evidence against such presumption) that certain acts or contracts damage the insolvency estate (eg, the creation of security in favour of pre-existing obligations, or contracts entered into with specially related persons (among others, shareholders owning more than 5 per cent of listed companies (or 10 per cent if not listed) or directors)). Refinancing agreements that meet the requirements provided for in the Insolvency Act are excluded from the general rescission regime and can only be challenged by the receivers on other grounds (eg, fraud).	
<b>Operating and financing during reorganisations</b>	
Depending on the specific regime decided by the court, the debtor might be able to enter into operations within the ordinary course of business. Any other transactions should be agreed by the court. Loan agreements accelerated prior to the insolvency declaration can be rehabilitated by the court.	
<b>International cooperation and communication</b>	
Both EU Regulation 1346/2000 and Regulation (EU) 2015/848 (the Recast Regulation) on cross-border insolvency proceedings, as well as the Insolvency Act establish the duty of reciprocal cooperation for domestic and foreign receivers. The Recast Regulation has introduced a completely new voluntary regime for group coordination that encourages members of a group to consider whether possibilities exist for restructuring the group and to coordinate a restructuring plan. A new regime to improve coordination and communication between receivers and courts has also been established by the Recast Regulation.	
<b>Liabilities of directors and officers</b>	
Directors may be liable for the harm caused as a result of actions or omissions that are contrary to the law or to the by-laws or that are in breach of the duties inherent to their position. Directors may also be liable if the company ceases to comply with certain subscribed capital-to-equity ratios and such ratios are not re-established within certain periods, in which case directors are under a legal duty to procure the winding up or (if applicable, the insolvency) of the company. The insolvency court may declare the director liable if the insolvency is classified as 'guilty'. The Spanish Criminal Code includes a number of criminal offences that may apply to a director. Pending legislation	
<b>Pending legislation</b>	
Law 9/2015 includes an additional provision which enables the Spanish Government to elaborate a Restated Text of the insolvency legislation. A new Royal Decree on receivers' legal regime is pending approval.	

SWEDEN	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Swedish Bankruptcy Act (SFS 1987:672), Right of Priority Act (1970:979), Reorganisation of Business Act (1996:764). More than 95 per cent of the cases are liquidations and only 5 per cent, or even less, are business reorganisations. However, also under a liquidation the business can be transferred to a new entity and survive.
	<b>Customary kinds of security devices on immoveables</b>
	Security interest in real property, ships and aircraft is created by mortgaging.
	<b>Customary kinds of security devices on moveables</b>
	The principal types of security devices that are taken on moveables are: pledges; security assignments; reservation of title; and floating charge in the changing assets of a business enterprise.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	<b>Bankruptcy</b> Generally a creditor's pecuniary claim should be filed and tested in the bankruptcy proceedings and only a creditor holding a pledge (including mortgages) is allowed to continue execution procedures (through the Enforcement Authority). Sale of pledged assets except through the Enforcement Authority is restricted in several ways and may need the consent of the trustee. Property that is not pledged or mortgaged, including assets to which a creditor has security interest in way of a floating charge, is sold by the trustee.
	<b>Business reorganisation</b> The opening of such proceedings does not stay legal proceedings as such. The opening of a business reorganisation is intended, inter alia, to prevent independent actions by one or more of the creditors. Therefore, a petition for bankruptcy filed by a creditor after the commencement of a case is, with some exceptions, to be declared suspended and execution proceedings, not relating to claims secured by a pledge, are stayed.
	<b>Duties of the insolvency administrator</b>
	The general duties of the trustee in bankruptcy is to wind up the company, collect the assets and distribute the funds among the creditors in the most prompt and favorable way for the creditors as possible. The administrator in business reorganisation proceedings is under a duty to examine the debtor's affairs, assess the possibilities to continue the company's operations and negotiate with the creditors on a reorganisation plan as well as a possible composition.
	<b>Set-off and post-filing credit</b>
	Set-off is, with some exceptions, allowed in bankruptcy and reorganisation proceedings if the claim and counterclaim existed at the day of the opening of the proceeding. Post-filing credit can be obtained and will normally be preferential.
	<b>Creditor claims and appeals</b>
	If the trustee is able to ascertain which creditors are entitled to payment in the bankruptcy, the creditors only need to notify the trustee of their claims. In more complicated bankruptcies proofs of debt must be filed with the court. The court of first instance is the district court, whose decisions maybe appealed to the Court of Appeal and ultimately the Supreme Court. There is no formal procedure of lodging claims in public business reorganisation proceedings, but the administrator must be notified of the claim before the date of the creditors' meeting. The debtor, the administrator and other creditors may object to a specific claim.
	<b>Priority claims</b>
	Priority claims should be paid in the following order: preferential rights in respect of certain specific property; preferential rights in certain non-specific property; and employees' salary claims, etc. Claims against the bankrupt estate itself must always be paid before other claims.
	<b>Major kinds of voidable transactions</b>
	Transactions whereby a creditor has been improperly favoured as against others; gifts; unreasonably high salary payments; payments of debts within a certain period before the limitation date made by non-customary means; and conveyance of security within a certain period prior to the limitation date. The recovery provisions in the Bankruptcy Act also apply in a business reorganisation situation.
	<b>Operating and financing during reorganisations</b>
The debtor retains control over its property but must consult the administrator. The debtor, with the consent of the administrator, is allowed to raise new loans during the business reorganisation in order to facilitate the reorganisation. Such new credit has a favorable priority in any following bankruptcy, provided that the specific agreement has been entered into during the reorganisation with the administrator's consent.	
<b>International cooperation and communication</b>	
There are no certain rules regarding international cooperation and communication besides the rules contained in the EC Regulation.	
<b>Liabilities of directors and officers</b>	
Personal liability of directors may arise under the provisions in the Companies Act and the company directors may also be personally liable for unpaid taxes and duties if they have negligently failed to pay them. In addition, there are rules on criminal liability of directors as well as rules on trade prohibitions.	
<b>Pending legislation</b>	
A new regulation regarding debt reconstruction for individuals will become effective on 1 November 2016. The new regulation will make it possible for more people to apply for and undergo debt restructuring and will include a certain possibility for business owners.	

<b>SWITZERLAND</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	The Federal Statute on Debt Collection and Bankruptcy (DCBA) governs the enforcement of pecuniary claims and claims for the furnishing of security against private individuals and legal entities of private law.
	<b>Customary kinds of security devices on immoveables</b>
	Security interests in real property, ships and aircraft by way of a mortgage.
	<b>Customary kinds of security devices on moveables</b>
	Pledges, right of retention, retention of title, fiduciary transfer of property title (in particular assignment of claims).
	<b>Stays of proceedings in reorganisations/liquidations</b>
	The commencement of composition and bankruptcy proceeding automatically stays almost all execution proceedings. Except for urgent matters civil court proceedings will be suspended.
	<b>Duties of the insolvency administrator</b>
	During the composition agreement the administrator supervises the business of the debtor, examines the affairs and submits its recommendation regarding the reorganisation plan to the court. In liquidation he marshals and liquidates the assets for distribution to the creditors according to the creditors' schedule.
	<b>Set-off and post-filing credit</b>
	Set-off is permitted except in cases considered as misuse. The debtor is either prevented (bankruptcy) or restricted (composition) from disposing of its assets. The administrator has to consent to contract new obligations, such as loan or credit, which may touch its assets.
	<b>Creditor claims and appeals</b>
	Creditors must submit their claims within a month after the public announcement of commencement of a composition or a bankruptcy. The disallowance of its claim can be challenged by the creditor by instituting legal proceedings.
	<b>Priority claims</b>
	Three different classes are distinguished: first class: claims of employees that arose during the six months prior to the opening of proceedings and unpaid pension plan contributions; second class: unpaid social security contributions; and third class: all other claims (including taxes).
	<b>Major kinds of voidable transactions</b>
Gifts (and equivalent transactions), preferential transactions concluded in over-indebted situation; fraudulent transactions.	
<b>Operating and financing during reorganisations</b>	
Under the supervision of the commissioner the debtor may continue its business operations, however certain transactions will require court approval or approval of the creditors' committee. Transactions approved by the administrator (and the court or creditors' committee when necessary) enjoy privileged treatment.	
<b>International cooperation and communication</b>	
Foreign insolvency administrators require approval by the relevant Swiss authorities to represent the foreign insolvent estate for assets located in Switzerland (application for ancillary ('mini') insolvency proceeding). No specific rules are established for international cooperation; official secrecy rules will be observed. A language barrier may be encountered. Special rules apply for insolvency proceedings involving regulated financial institutions.	
<b>Liabilities of directors and officers</b>	
Any member of the board of directors or any person entrusted with management (officers) is liable for any damage caused in the corporation, its shareholders or creditors where he or she has intentionally or negligently acted in breach of his duties. They may also become liable for unpaid social security or certain taxes.	
<b>Pending legislation</b>	
Proposed revision of Swiss company law including a new early warning system according to which members of the board of directors are required to prepare a cash flow forecast if there is reasonable doubt that the company remains solvent over the next 12 months. It is still uncertain if and when this revision will come into force. A legislative proposal is pending to modernise the recognition of foreign bankruptcy and like orders (See Update and trends.)	

<b>THAILAND</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Bankruptcy Act BE 2483 (AD 1940). Bankruptcy Court Act BE 2542 (AD 1999). Regulations for Bankruptcy Cases BE 2549 (AD 2006).
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage.
	<b>Customary kinds of security devices on moveables</b>
	Pledge and retention.
	<b>stays of proceedings in reorganisations/liquidations</b>
	Automatic stay is available only in reorganisation under section 90/12 of the Bankruptcy Act BE 2483 (AD 1940).
	<b>Duties of the insolvency administrator</b>
	In bankruptcy, the official receiver must gather the assets of the debtor and distribute them among the creditors. In reorganisation, the plan administrator plays the said role in compliance with the reorganisation plan.
	<b>set-off and post-filing credit</b>
	Creditors can set-off debts, unless the creditor's right of claim against the debtor is accrued after the court's order of receivership or after the court's order of a reorganisation. Upon the issuance of the court's order of receivership, a debtor is prohibited from doing any acts relating to the asset, or the business, except by order or approval of the court, the official receiver, the administrator of the asset, or of a creditors' meeting (as the case may be). Otherwise, the transaction will be void. Once the court orders acceptance of the reorganisation petition, the debtor is prohibited from undertaking certain activities during the term of automatic stay.
	<b>Creditor claims and appeals</b>
	The application for repayment of debt is submitted to the official receiver. In bankruptcy proceedings, the appeal of the court's order with respect of the repayment of debt is made to the Supreme Court, Bankruptcy Division. In reorganisation proceedings, the appeal of the official receiver's order with respect of the repayment of debt is made to the court.
	<b>Priority claims</b>
	Bankruptcy: Official receiver's fees, court fees and taxes due for payment within six months prior to the bankruptcy order; secured creditors with regard to secured assets; and employees. Reorganisation: In accordance with the plan, but if a priority creditor is treated other than in accordance with the normal distribution rules, that creditor must give its consent; if the reorganisation order is revoked and the debtor is declared bankrupt, debts incurred by the official receiver, planner and plan administrator have priority equal to the expenses of the official receiver in bankruptcy.
	<b>Major kinds of voidable transactions</b>
	Fraudulent transfer and preferential transfer.
	<b>Operating and financing during reorganisations</b>
	Operating and financing during reorganisation which is conducted in the ordinary course of business can be done under the Bankruptcy Act BE 2483 (AD 1940).
<b>International cooperation and communication</b>	
None at present.	
<b>Liabilities of directors and officers</b>	
The liability of the directors and officers is separated from the liability of the company.	
<b>Pending legislation</b>	
None at present.	

<b>TURKEY</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Bankruptcies and reorganisations are generally governed by the Enforcement and Bankruptcy Law (EBL) numbered 2004.
	<b>Customary kinds of security devices on immoveables</b>
	Mortgage.
	<b>Customary kinds of security devices on moveables</b>
	Pledge, right of retention, commercial enterprise pledge.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	The commencement of restructuring and bankruptcy proceeding automatically stays almost all execution proceedings.
	<b>Duties of the insolvency administrator</b>
	They manage the bankruptcy estate and liquidate the assets for distribution to the creditors according to the creditors' ranks.
	<b>Set-off and post-filing credit</b>
	Set-off is permitted except in cases considered as abuse. As the debtor is generally restricted from disposing of its assets, credit may only be obtained with the consent of the trustee or commissar. No credit can be obtained during bankruptcy liquidation.
	<b>Creditor claims and appeals</b>
	Creditors must register their claims within a month of the public announcement of commencement of a bankruptcy. Creditors may appeal the decisions of the bankruptcy administration with respect to their ranks or rejected amounts.
	<b>Priority claims</b>
	Four different ranks are distinguished: first rank: claims of employees, unpaid pension plan contributions and alimony receivables; second rank: guardian and ward claims; third rank: privileged claims accepted based on their own laws (including taxes and all other public receivables); and fourth rank: all other claims.
	<b>Major kinds of voidable transactions</b>
Voluntary acts of disposal during the last two years prior to the commencement of bankruptcy liquidation; an act of disposal performed in case of insolvency; acts of disposal intentionally performed for the purpose of causing damage.	
<b>Operating and financing during reorganisations</b>	
Under the supervision of the commissar or trustee the debtor may continue its business operations.	
<b>International cooperation and communication</b>	
No specific rules are established for international cooperation and communication.	
<b>Liabilities of directors and officers</b>	
The personal responsibilities of the managers arise if their obligations are violated. This responsibility will also be valid with regard to the public receivables.	
<b>Pending legislation</b>	
None at present.	

<b>UNITED ARAB EMIRATES</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Federal Law No. 18 of 1993 (Commercial Code). Federal Law No. 2 of 2015 (Companies Law). Federal Law No. 5 of 1985 (Civil Code). Federal Law No. 11 of 1992 (Civil Procedure Code). Federal Law No. 10 of 1980 (Central Bank Law).
	<b>Customary kinds of security devices on immoveables</b>
	Mortgages.
	<b>Customary kinds of security devices on moveables</b>
	Business mortgage (pledge over a commercial business). Pledge.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	Proceedings can only be continued with permission of the court.
	<b>Duties of the insolvency administrator</b>
	The trustee is responsible for issuing notices providing reports to creditors and the court, gathering in assets and continuing the business where relevant.
	<b>Set-off and post-filing credit</b>
	Set-off requires connection between the obligations.
	<b>Creditor claims and appeals</b>
	Local creditors and the debtor have 10 days. Creditors based outside the UAE generally have 30 days.
	<b>Priority claims</b>
	Priority given to employee salaries, government taxes, rent on business premises, secured creditors and bankruptcy costs and expenses.
	<b>Major kinds of voidable transactions</b>
	Gifts, early repayments, debts paid with something other than as agreed, providing security for pre-existing debts and transactions that are detrimental to the creditors may be voided.
	<b>Operating and financing during reorganisations</b>
	Subject to court permission initially. Continuance of business after a judicial composition is subject to approval by the creditors During a protective composition permission of the creditors is required before the debtor can obtain financing.
<b>International cooperation and communication</b>	
There are no provisions in UAE law that facilitate international cooperation and communication in the context of insolvencies.	
<b>Liabilities of directors and officers</b>	
Directors and offices may be liable for: <ul style="list-style-type: none"> <li>• acts of fraud;</li> <li>• abuse of power;</li> <li>• violation of law or constitutional documents; and</li> <li>• mismanagement of the company;</li> </ul> Risk of criminal penalties for fraudulent actions.	
<b>Pending legislation</b>	
A new federal insolvency code remains under discussion but dates for publication of a draft have yet to be disclosed.	

<b>UNITED STATES</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Title 11 of the United States Code (Chapter 7 governs liquidations; Chapter 11 governs reorganisations).
	<b>Customary kinds of security devices on immoveables</b>
	The real estate mortgage. Alternative forms include the land sale contract and deed of trust.
	<b>Customary kinds of security devices on moveables</b>
	Security interests created under and enforced by article 9 of the UCC. Special security devices exist for certain intangible property, equipment such as automobiles, aeroplanes, etc, and intellectual property.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	The filing of a bankruptcy petition immediately triggers an automatic stay that enjoins most creditor enforcement action against the debtor and its property.
	<b>Duties of the insolvency administrator</b>
	The trustee or debtor-in-possession is an officer of the court and has a fiduciary duty to protect and preserve assets of the estate, and to administer such assets in the best interests of creditors.
	<b>Set-off and post-filing credit</b>
	Bankruptcy generally does not affect set-off rights existing under non-bankruptcy law, but relief from stay must be obtained. Unsecured and secured post-petition credit may be obtained with court approval.
	<b>Creditor claims and appeals</b>
	Creditors generally file proofs of claim. Disputes are litigated in the bankruptcy court (or other court of competent jurisdiction) and may be appealed.
	<b>Priority claims</b>
	Expenses of administering the estate and other specified claims such as wages, pension benefits, and certain taxes enjoy priority.
	<b>Major kinds of voidable transactions</b>
	Fraudulent and preferential transfers may be avoided.
<b>Operating and financing during reorganisations</b>	
The debtor-in-possession may operate its business in the ordinary course. Court approval must be obtained for transactions outside the ordinary course of business.	
<b>International cooperation and communication</b>	
Chapter 15 of the Bankruptcy Code codifies the UNCITRAL Model Law on Cross-Border Insolvency, with some modifications. Chapter 15 enables a foreign representative of a foreign estate to obtain US bankruptcy court recognition of a foreign proceeding and thereby access a panoply of relief with respect to the foreign debtor's assets and operations in the US, including the imposition of the automatic stay, administration of the foreign debtor's US assets and operation of the foreign debtor's US business. The statute authorises and encourages communication between and among US and non-US courts.	
<b>Liabilities of directors and officers</b>	
Corporate directors and officers generally have no personal liability unless they have breached their fiduciary duties. Such duties expand to include the interests of creditors upon or near insolvency.	
<b>Pending legislation</b>	
Among other things, proposed legislation was introduced in the US to address the growing student loan debt, as well as Puerto Rico's financial troubles. None of the legislation has been passed by both houses of Congress or enacted into law.	

<b>Vietnam</b>	<b>Applicable insolvency law, reorganisations: liquidations</b>
	Bankruptcy Law 2014. Enterprise Law 2014, applied to voluntary liquidation out of the court-driven insolvency proceedings.
	<b>Customary kinds of security devices on immoveables</b>
	A mortgage.
	<b>Customary kinds of security devices on moveables</b>
	A mortgage or a pledge.
	<b>Stays of proceedings in reorganisations/liquidations</b>
	After the court's acceptance of the bankruptcy petition, except for limited exceptions, the following are suspended: (i) civil, business, commercial or labour legal proceedings; (ii) enforcement a court/arbitral judgment, award or decision; (iii) enforcement of security over assets.
	<b>Duties of the insolvency administrator</b>
	An asset management officer or firm (the receiver) appointed by court to play a role similar to that of a receiver in bankruptcy proceedings or liquidator in case of liquidation.
	<b>Set-off and post-filing credit</b>
	A set-off is generally permitted and, subject to certain limitations, a debtor may incur debts after the filing of the bankruptcy petition.
	<b>Creditor claims and appeals</b>
	Claims of creditors must be sent to the receiver, and the list of creditors must be finalised thereafter, within a fixed time frame.
	<b>Priority claims</b>
	Priority claims include (i) bankruptcy costs and expenses; (ii) payment to employees; and (iii) post-filing debts for the purpose of business recovery.
	<b>Major kinds of voidable transactions</b>
Voidable transactions include: (i) transfer of property not at market price; (ii) conversion of an unsecured debt into a secured debt; (iii) making payments or setting off an obligations under terms in favour of a creditor; (iv) donation of assets; (v) transaction outside the scope of business; and (v) transactions for the purpose of 'dispensing' assets.	
<b>Operating and financing during reorganisations</b>	
Subject to the approved recovery plan.	
<b>International cooperation and communication</b>	
Orders, decisions and judgments of most of the courts of developed jurisdictions are generally not recognised in Vietnam.	
<b>Liabilities of directors and officers</b>	
Officers and directors will not generally be personally liable for obligations of their company, except that they act ultra vires or breach fiduciary duties.	
<b>Pending legislation</b>	
Not applicable.	

## Getting the Deal Through

Acquisition Finance  
Advertising & Marketing  
Agribusiness  
Air Transport  
Anti-Corruption Regulation  
Anti-Money Laundering  
Arbitration  
Asset Recovery  
Aviation Finance & Leasing  
Banking Regulation  
Cartel Regulation  
Class Actions  
Commercial Contracts  
Construction  
Copyright  
Corporate Governance  
Corporate Immigration  
Cybersecurity  
Data Protection & Privacy  
Debt Capital Markets  
Dispute Resolution  
Distribution & Agency  
Domains & Domain Names  
Dominance  
e-Commerce  
Electricity Regulation  
Energy Disputes  
Enforcement of Foreign Judgments  
Environment & Climate Regulation  
Equity Derivatives  
Executive Compensation & Employee Benefits  
Financial Services Litigation  
Fintech  
Foreign Investment Review  
Franchise  
Fund Management  
Gas Regulation  
Government Investigations  
Healthcare Enforcement & Litigation  
High-Yield Debt  
Initial Public Offerings  
Insurance & Reinsurance  
Insurance Litigation  
Intellectual Property & Antitrust  
Investment Treaty Arbitration  
Islamic Finance & Markets  
Labour & Employment  
Legal Privilege & Professional Secrecy  
Licensing  
Life Sciences  
Loans & Secured Financing  
Mediation  
Merger Control  
Mergers & Acquisitions  
Mining  
Oil Regulation  
Outsourcing  
Patents  
Pensions & Retirement Plans  
Pharmaceutical Antitrust  
Ports & Terminals  
Private Antitrust Litigation  
Private Banking & Wealth Management  
Private Client  
Private Equity  
Product Liability  
Product Recall  
Project Finance  
Public-Private Partnerships  
Public Procurement  
Real Estate  
Restructuring & Insolvency  
Right of Publicity  
Securities Finance  
Securities Litigation  
Shareholder Activism & Engagement  
Ship Finance  
Shipbuilding  
Shipping  
State Aid  
Structured Finance & Securitisation  
Tax Controversy  
Tax on Inbound Investment  
Telecoms & Media  
Trade & Customs  
Trademarks  
Transfer Pricing  
Vertical Agreements

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