# Position Paper

## UEAPME[1] position on an efficient insolvency framework within the EU.

### Introduction

The European Commission has launched a public consultation on an effective insolvency framework within the European Union. The consultation includes questions on which the measures would be necessary, how the legislation of member states affects the proper functioning of the internal market, early restructuring, restructuring procedures, debt discharge following a bankruptcy and several individual questions such as recovery, ranking of claims, duration of proceedings and disqualification.
UEAPME once again regrets that the consultation is done through a compulsory questionnaire which is not an appropriate instrument for European associations which have to find agreed positions. This position paper is the only way UEAPME will reply to this consultation and it will be sent to the Units in charge of the file.

### 1. Scope

As stated in the Commission's consultation, a good insolvency framework promotes effective and predictable insolvency proceedings.
The different measures that could and should be taken to achieve an appropriate insolvency framework within the EU are known: Preventive measures to enable the restructuring of viable businesses; Measures to increase the recovery rates of debts in insolvency; Measures to ensure the discharge of debts for entrepreneurs; Measures to ensure the discharge of debts for consumers; Measures governing employees' rights in insolvency; Measures ensuring the enforcement of debts.

To achieve such an adequate insolvency framework, UEAPME emphasises, that preventive measures that help viable companies to enter restructuring must be the primary consideration in the development of insolvency proceedings and are the most important ones. Indeed on the condition that a business is viable, it is of the upmost importance that a business in difficulty should be detected early enough, and be offered adjusted assistance. This assistance could be offered in the form of restructuring, but the aim of preventive measures should focus on businesses in difficulties that can be helped without having to resort to restructuring measures. If the survival of the business can be achieved without restructuring measures, the impact on creditors and employees is kept to a minimum. In case of restructuring measures, a fair balance between the survival of the business on the one hand, and the rights of the creditors on the other should be guaranteed.

[1] UEAPME subscribes to the European Commission's Register of Interest Representatives and to the related code of conduct as requested by the European Transparency Initiative. Our ID number is 55820581197-35.



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Well-functioning insolvency systems have economic significance. It is about the effectiveness of the operation of the market, the efficient use of economic resources, the tying up of public expenditure, as well as investor sentiment. The development of the insolvency systems of the Member States support the creation of a Capital Markets Union and its objectives.

Comparing national insolvency systems can be used to make peer pressure for Member States whose insolvency systems are not efficient. By means of recommendations it is possible to address emerging problems in the systems of each Member State. These recommendations have been made and will continue to provide the framework of the economic policies of the Semester. Harmonisation of certain aspects of insolvency law will not increase their effectiveness or lead to significant effects, especially when the efficiency of the problem is due to factors related to the functioning of the justice system.
The national insolvency laws form a coherent whole, which is largely linked to the rest of the national legal framework, the corporate culture, the payment behaviour and general attitude climate.
The targets proposed by the Commission are good and in the right direction, but they should not lead to a comprehensive harmonisation of legislation. Harmonisation of certain aspects and the introduction of "foreign" elements in the national system may impair the operation of the system as a whole. The improvement of insolvency systems must take into account the systems as a whole and the different parties involved- from the perspective of companies, the different position of creditors and customers.
UEAPME stresses the importance of a comprehensive impact assessment before proposing any new measure. The economic impact of the proposal, as well as the effects of insolvency proceedings on the different parties concerned should be assessed thoroughly.
Moreover, all measures should take the "Think Small First" principle into account.

Most of our organisations and enterprises have no extensive experience with cross - border restructuring or insolvency proceedings but in our opinion the existing differences between the laws of the Member States do not really affect the functioning of the Internal Market, as businesses are not in competition via insolvency law. There can be eventually an impact on creditors and investors who have to take into account the legislation on the recovery of debts before starting financial or commercial relations in another country.

**Impact on newly created businesses**

Insolvency law is – as the whole legal framework – of importance for the environment in which business establishments take place The extent of the impact of preventive measures to enable the restructuring of viable businesses depends on the kind of 'preventive measures'. Restructuring measures will probably have a rather small direct impact on start-ups. But preventive measures in the form of more emphasis on a thorough business plan and on entrepreneurial skills will have a direct impact.

Concerning the impact of measures to increase the recovery rates of debts in insolvency, we would like to remark that in some cases, start-ups have a smaller client - base as well as a smaller financial buffer than "older" companies. Consequently the insolvency of a client might have a larger impact on start-ups. The possibility of discharge of debts on the contrary, will not affect start-ups more than other companies.

Measures ensuring the adequate enforcement of debts are obviously important for all companies, not only start - ups. But since the financial buffer of start-ups might be more limited than that of older companies, the enforcement of debts might be more important to start-ups.


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## 2. Saving viable businesses in difficulty

Concerning restructuring and rescuing companies in difficulty, it is essential that insolvency regulation is not made too strict. In UEAPMEs view, focusing on measures that create efficient systems and procedures for implementation of restructuring is important. Measures that offer assistance for debtors in financial difficulty are particularly crucial for small enterprises and entrepreneurs. Developing better and uniform proceedings that facilitate assessment of companies' viability in the event of insolvency both nationally and on EU level is an appreciated objective.

It is important that insolvency proceedings in all Member States operate efficiently and allow for the reorganization of viable businesses, as well as the highest possible degree of recovery of debts. This should be by means that are as effective as possible. The Union's measures are justified if the objectives cannot be sufficiently achieved by the Member States and of the scale or effects of the proposed action, be better achieved at Union level.

On the Internal market aspect, the availability of relevant information about the insolvency law applicable is important as well as to ensure the assessment of a debtor's viability.
Council Directive 2001/23/EC of 12 March 2001 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 reduces opportunities to save businesses and jobs at times.

Concerning the impact the different types of possible measures have on saving viable businesses, measures to ensure the assessment of the viability of a debtor are certainly of utmost importance, but the impact will of course depend on the criteria that are used for the assessment. The measures to lay down the duties of directors in companies in financial distress should not be too strict, but they are nevertheless very important. The director should be the first one to detect problems and act on them. The earlier he/she detects financial problems and the better he/she acts on them, the higher the chances of recovery.
Measures to protect new financing given to companies that are being restructured could be very important, but again the question will be what is regarded as 'new financing'. Very often, financing is given by a delay in payment, which should have the same protection as financing from a bank.
Measures to promote assistance to financially distressed debtors can have also an impact on saving valuable enterprises but obviously, this will depend on the kind of measures (but it is not entirely clear what kind of measures are envisaged in question 2.2.).

A debtor should have access to restructuring measures before the debtor is insolvent. However, measures requiring a stay on enforcement actions, should be limited. The focus should be directed towards other forms of assistance. The debtor should only have access to restructuring measures that require a moratorium when it is absolutely necessary, Publicity should only be required when the restructuring measures affect all creditors (because in that case it is important that all creditors are informed of the restructuring measures). However, if the restructuring measures only affect certain creditors and not all, publicity of the financial troubles would only alarm creditors that are not involved in the restructuring measures, which could have a negative impact on the financial position of the debtor. Publicity can indeed worsen the position for companies in financial distress, damaging the brand and providing competitors an opportunity to take advantage. This would limit opportunities for recovery.

The involvement of a court should always be obliged when the restructuring measures (might) have an impact on creditors without their consent (for example "cram down" procedures). The level of involvement of the court should depend on the kind of measures. For example; if the restructuring measures only affect certain creditors, and the debtor finds an agreement with these creditors, the court should be able to confirm this agreement, without having to be involved in every stage of the proceedings.



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Whether or not debtors in the context of restructuring measures should be able to keep control over the day-to-day operations of their business (so-called 'debtor-in-possession arrangements'), should depend on the kind of restructuring measures. In case of a stay on enforcement measures, where the rights of creditors are otherwise limited, at least a supervision on the day-to-day operations should be required. However, if no rights of creditors are limited, the debtor should maintain control.

Debtors should be able to ask for a stay of individual enforcement actions in formal insolvency proceedings and in preventive/pre-insolvency restructuring procedures. They should not be the general rule, but they should nontheless be possible.
Once the restructuring attempts are ongoing, the enforcement of actions of individual creditors should be stayed during any time limit set by the court subject to the fulfilment of certain conditions. It should be the prerogative of the court to determine the length of a stay on enforcement actions, based on the facts of the case. The decision of the court will take all facts into consideration, hence it will be fairer for all.

An individual creditor should be allowed to ask the court to lift the stay granted to the debtor in certain cases and subject to certain conditions (for example when it is clear that the debtor has only started a procedure to avoid a claim of the individual creditor).

A restructuring plan adopted by the majority of creditors could be binding on all creditors provided that it is confirmed by a court under three conditions:
1) The procedure in which it is possible to enforce a restructuring plan on all creditors should only be accessible to a business in difficulty as a 'last resort' (when it is impossible for them to restructure using less far reaching measures).
2) The confirmation of a court is absolutely necessary, and the court should have a legal obligation to take into consideration the effects of the confirmation of such a plan on the creditors that voted against the plan.
3) Creditors should be entitled to a minimum of their claim.

According to UEAPME[2]', a 'cross-class cram down' (i.e. the confirmation of the restructuring plan supported by some classes of creditors in spite of the objections of some other classes of creditors), should be possible under the same three conditions mentioned above.

In theory directors of companies should be incentivised to take appropriate preventive measures if companies are in distress but not yet insolvent, for example by being able to avoid related liability.
However, it would be crucial not to make these 'incentives' too strict. Liability of directors of companies is a delicate subject, in which a balance has to be found between enough incentives on the one hand (even in the form of liability), and a certain realism about the financial knowledge and capacities of directors in SME's.

Member States should be encouraged to take specific action to help all debtors in financial distress, such as setting up special funds or insurance systems covering the provision of cheap and accessible restructuring advice, possibly subject to certain conditions.

2 With the exception of WKÖ



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## 3. Second chance[3]

Studies have shown that second-chance entrepreneurs are more successful and operate for longer than start-ups, in addition to experiencing quicker growth and employing more workers. Against this background, the discharge of liability for an honest entrepreneur and giving a 'second chance' are welcome and legitimate. UEAPME considers it important that over indebted honest debtors are enabled debt settlement and therefore a discharge of liability.

Both entrepreneurs and consumer who are over-indebted should have the possibility to restructuring their debt, but only if they have tried other, less far reaching, options.
Over-indebted individuals, entrepreneurs (individuals) and consumer should have access to free or low cost debt advice, possibly subject to certain conditions.
A full discharge of debts for businesses (natural persons) and consumers should only be offered under certain preconditions which sustainably prevent misuse of this instrument and be limited to situations of honest bankruptcy, but only if a restructuring plan is no longer an option. It should also not necessary apply to the whole debt.
On the maximum discharge period we are of the opinion that the shorter the period, the more difficult it is for the debtor to fulfill the requirements. But in case of a bankruptcy the honest debtor should be discharged within a period of one[4] year, unless the court decides that this period is not sufficient in light of the complexity of the case. We are also of the opinion that if it is decided that the discharge of debts should be offered to all individuals, whether entrepreneurs or consumers, the conditions for the discharge be the same

## 4. Increasing the efficiency and effectiveness of the recovery of debts

It is necessary to further emphasise that the earlier possible insolvency situations are addressed and the earlier the debtor has available information on the opportunities and framework of restructuring, the better the chances to avoid 'unnecessary' insolvency. Secondly, it is essential that voluntary and informal procedures are developed alongside official, statutory insolvency proceedings.

However, the release of debts should not be subjected to debtors whose debt can be considered blameworthy occurred. Still, at EU level should not be set what type of reprehensibility should prevent debt restructuring.
Effective insolvency legislation promotes efficient management of non-payments, as concluded in the consultation. The consultation also refers to Commission Communication 'Towards the Completion of the Banking Union' of 24 November 2015, which argued that effective insolvency legislation would increase recovery rates of non-performing loans. UEAPME considers it important that insolvency legislation safeguards the rightful position of creditors, and that there are efforts to tackle difficulties in recovery of problem debts. Here we would, however, like to underline that UEAPME does not consider legislation appropriate, in which some creditor groups, such as financial institutions, would be granted a special priority in insolvency proceedings any more than currently provided. In our opinion this could lead to deterioration of both debtor and creditor companies. It should be noted as well that banks and other financial institutions are already in effect in better positions than small creditors, generally due to securities required for financing.
So in our view it is important that the degree of recovery of debts raised and improve the efficiency of procedures. In this respect, it should be clarified in more detail the means by which the objective can best be achieved.

3 This part on Second chance represents the views of UEAPME with the exception of its member WKÖ.
4 With the exception of ZDH.



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To improve recovery harmonization of insolvency law is not the solution. At EU level it should not adjust the ranking of creditors. The ranking is also strongly coupled to other national legislation and the national system issue that cannot be addressed in isolation from the rest of the legislation. Again it is important that functioning of the existing regulation is reviewed before the new legislative measures.

UEAPME would like to point out that insolvency legislation and procedures should be developed so, that companies would be better directed to appropriate insolvency proceedings.
It is important to review both nationally and on EU level how different procedures meet the needs of enterprises of varying sizes. Restructuring procedure, for instance, is possible for all enterprises, but in practice it is too burdensome and expensive for a small business trying to overcome a financial crisis. What is more, a restructuring procedure is too lengthy. It takes almost a year in most cases from filing the restructuring to the confirmation of the programme. Insolvency proceedings should be made more efficient in future to enable immediate start of possible restructuring and to shorten the duration of the procedure itself.
The future objective should be to shift the focus of insolvency proceedings away from liquidation of business in such a way that financially viable enterprises are encouraged to implement restructuring at an early stage to prevent insolvency. In accordance with these principles, the objective of the development of insolvency legislation has to be solving debt problems in a way that is quicker, fairer and more cost-effective than it currently is.
Finally, the disqualification should not be circumvented by engaging in activities in another Member State or in another Member State. In this regard, the mechanisms for exchange between Member States of information relating to business bans should be reviewed in order to improve transmission of relevant details and reduce the potential for banned individuals to simply transfer their activities. However, the issue is not related to the insolvency proceedings, and it should therefore be considered in isolation, also taking into account data protection aspects.

The different measures, mentioned in the questionnaire (Minimum standards on the ranking of claims in formal insolvency proceedings; Minimum standards on avoidance actions; Minimum standards applicable to insolvency practitioners/mediators/supervisors; Measures providing for a specialisation of courts or judges; Measures to shorten the length of insolvency proceedings; Measures to prevent disqualified directors from starting new companies in another Member State) do not contribute to increase the recovery rate of debts. In case of an insolvency procedure, the chances of recovering a debt are virtually not existing. For that reason, it is important to give businesses access to other measures, such as restructuring proceedings.

Secured creditors should be satisfied in principle before all other creditors.

A target maximum duration of insolvency proceedings — either at first instance or including appeals would be appropriate, but with the possibility of exemptions in case of complicated proceedings.

When disqualification orders for directors are issued in one Member State (i.e. the 'home State'), they should automatically prevent disqualified directors from managing companies in other Member States

Directors disqualified in one Member State (home State) should be prevented from managing companies in other Member States only for the duration applicable to equivalent disqualification orders in the host State.

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