5. Chapter 5: Exposition of the Preventive Restructuring Directive

5.1 Introduction

5.1.1 Context of Exposition within the JCOERE Project

Chapter 5 of this Report provides a detailed exposition of the evolution of the Preventive Restructuring Directive,[1] which at the commencement of the JCOERE Project was still only a Proposal for a Directive on Preventive Restructuring.[2] As the PRD came into effect on 20th June 2019 and has now entered the implementation period, which is due to end on 17th July 2021,[3] this task became more challenging. However, this challenge allowed the JCOERE Project team the opportunity to fully assess the institutional changes that occurred prior to the finalised PRD with a clear picture of the compromise eventually achieved. This legislative process adumbrated the difficulties that there may be in the harmonisation of implementation of the PRD across the Member States, given the competing values apparent in the final drafting. This Chapter will describe the progress of the Directive through various EU Institutions and will highlight the significant changes that have occurred along the way, providing a background against which the contributor responses to the JCOERE Questionnaires can be discussed in Chapters 6, 7, and 8.

5.1.2 Presentation of the Chapter

The journey of the PRD began in 2011 going through many levels of EU negotiations until finding its current state as a Directive. The JCOERE Project has identified a collection of the provisions in the PRD that may present obstacles to judicial co-operation. These rules are also the subject matter of the JCOERE Questionnaire Mapping the Preventive Restructuring Frameworks and the EU Directive, the responses to which will be discussed and analysed in Chapters 6 and 7 of this Report. The articles of the PRD, upon which the JCOERE Project focuses are articles 6, 9, 10, 11, 13, and 17.

For the purpose of this Chapter, the conceptual foundations of these articles will be discussed as they developed over time and through various institutional changes into their final form.[4] These concepts include the stay of individual enforcement actions; the protection of new finance; decreased court formality; and the cross-class cram-down. The stay and the protection of new financing are clearly now enshrined in articles 6 and 17 respectively. The cross-class cram-down and its connected rules regarding the adoption and confirmation of restructuring plans are set out in articles 9-11, while article 11 contains the mechanics of the provision as well as some of its most controversial characteristics. Articles 9 and 10 will be discussed only insofar as they relate to article 11 in this Chapter. Finally, court involvement, whether this amounts to decreased court formality or otherwise depending on jurisdiction, is considered under article 4, but really is present as a concept in all of the aforementioned articles. This will be discussed insofar as it has developed within the various provisions. The conclusion of this Chapter will

[1] Directive (EU) 2019/1023 of the European Parliament and of the Council of June 20 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and the amending of Directive (EU) 2017/1132 (Directive on restructuring and insolvency) [2019] OJ L 172/18 (the "PRD").
[2] Proposal for a Directive of the European Parliament and of the Council COM(2016) 723 final of 22 November 2016 on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU [2016] 2016/0359 (COD) (the "Proposal").
[3] PRD, art 34.
[44] There was little discussion of art 13 on Workers during these interinstitutional negotiations as this appeared at a very late stage in the drafting, so will not form a focus of this Chapter.

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then offer a brief synopsis of how the articles under scrutiny have changed from the Proposal to the PRD.

Section 5.2 begins with the report presented by the Committee on Legal Affairs – a committee of the European Parliament – to the European Commission in 2011, continues with the Communication from the Commission to the Parliament in 2012 and concludes with the Recommendation and accompanying Impact Assessment put forward by the Commission in 2014. By detailing this 3-year process, the intention is to give a clear overview of the steps preceding the Commission Proposal in 2016. Accordingly, this Chapter is split into three distinct parts:

(i) Section 5.2 – the historical context of the Directive (pre-Proposal);
(ii) Section 5.3 – the Commission Proposal (2016); and
(iii) Sections 5.4 & 5.5 – the negotiation process for the final Directive (post-Proposal).

5.2 Historical Context

5.2.1 Committee on Legal Affairs Report (2011)[5]

In 2011, the Committee on Legal Affairs issued a series of recommendations on insolvency proceedings in the EU to the Commission and with that report, began a journey towards the final Directive and indeed towards elements of the Recast Insolvency Regulation of 2015.[6] Amongst the other reasons for the proposed changes contained within the 33 recitals, the Committee noted that:[7]

(i) the (then) variances between national insolvency frameworks could lead to "forum shopping" by businesses and as such, there was a need to prevent abuse in order to benefit the internal market;[8]

(ii) whilst full harmonisation was not possible, there some areas of insolvency law where harmonisation would be worthwhile and achievable;[9]

(iii) there was significant difficulty in insolvency proceedings where the process involved a group of companies. At that time, the commencement of multiple separate insolvency proceedings in different jurisdictions was likely, as opposed to a co-ordinated approach, which led to more monetary losses for the parties involved and greater impediments to recovery;[10]

(iv) the interlinking of national insolvency registers would allow relevant parties and courts to determine whether insolvency proceedings have been opened in another Member State; and[11]

(v) the (then) lack of harmonisation with regard to the ranking of creditors was problematic and that a higher priority for employees' claims was necessary.[12]

The report went on to suggest that the European Parliament advocated harmonisation in the following five areas:

- certain aspects of the opening of insolvency proceedings;

[5] European Parliament Committee on Legal Affairs, 'Report with recommendations to the Commission on insolvency proceedings in the context of EU company law' (2011) A7-0355/2011 ("Legal Affairs Report").
[6] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) OJ L 141/19 (the "EIR Recast").
[7] Much of the content of the recitals focused on employees and employment law, which are not considered to be particularly relevant to the conversation at hand, except for (v), which pertains to employees as a class or creditors.
[8] Legal Affairs Report, recitals A & B.
[9] Legal Affairs Report, recital C. Later in the Legal Affairs Report, it became apparent that the areas were certain aspects of the opening of insolvency proceedings and the filing of claims, aspects of avoidance actions and restructuring plans and the qualifications and role of liquidators.
[10] Legal Affairs Report, recitals P & Q.
[11] *idem* recital R.
[12] *idem* recital AB.

- certain aspects of the filing of claims;
- aspects of avoidance actions;
- general aspects of the requirements for the qualification; and
- work of liquidators and aspects of restructuring plans.

The Parliament considered that the conditions under which insolvency proceedings could be opened should be harmonised via directive. The report supported harmonisation of, amongst other areas, the ability of companies themselves to initiate insolvency proceedings, the timely initiation of proceedings in order to allow for rescue, and the ability of the debtor to open proceedings if they are insolvent or likely to be.[13] Part 1.5 of the report proposed harmonisation of aspects of restructuring plans, including that debtors and liquidators may present a restructuring plan as an alternative to complying with statutory rules, that such plans must contain all relevant information enabling creditors to make a decision and that the plan must be approved (or rejected) by the relevant court.[14] Also noteworthy is part 2.4., where the European Parliament considers that article 32 of the Insolvency Regulation[15] should provide for an unequivocal duty of communication and co-operation, not only between liquidators, but also between courts.

5.2.2 Commission Communication 'A New Approach to Business Failure' (2012)[16]

Following on from this report, the Commission responded to the Parliament in the form of a Communication, dated 12 December 2012. In this document, "A new European approach to business failure and insolvency", the Commission identified six key areas where national differences could create "legal uncertainty and an 'unfriendly' business environment". They cited second chance for honest entrepreneurs; discharge periods that discourage a second chance; different rules on opening proceedings leading to varying chances for restructuring; unfulfilled expectations of creditors for different categories of debtors; uncertainty regarding procedures to file and verify claims for creditors; and the promotion of restructuring plans. Of key importance to the Commission as evidenced by the section dedicated to it was the situation faced by small and medium enterprises (SMEs). The report noted the importance of giving businesses in that sector a second chance and suggested four key ways in which SMEs could be supported: prevention (of bankruptcy due to high cost of restructuring), second chance, out-of-court settlements, and in-court procedures.

The report concluded with the 'steps to be taken,' namely:

(i) Modernisation of the EU Regulation on insolvency proceedings;

(ii) Adoption of the European Entrepreneurship Action Plan;

(iii) Country-specific recommendations inviting Member States to update their insolvency laws;

(iv) Impact assessment of the differences in national insolvency laws; and

(v) Public consultation on the issues identified in the document.

5.2.3 Commission Recommendation and Impact Assessment (2014)[17]

Subsequent to the Communication to the Parliament, the Commission drafted a Recommendation dated 3rd March 2014 and entitled 'A new approach to business failure' and an accompanying Impact Assessment. It was the view of the Commission at that time that the EU was still facing the single largest economic crisis in its history and that consequently, improving the efficiency of insolvency laws was critical to supporting economic recovery, given the record numbers of bankruptcies across Member

[13] *idem* part 1.1.
[14] *idem* part 1.5.
[15] Council Regulation (EC) 1346/2000 of 29 May 2000 on insolvency proceedings [2000] OJ L 160/1 (the "EIR").
[16] Communication from the Commission to the European Parliament, the Council, and the European Economic and Social Committee COM(2012) 742 final of 12 December 2012 on a new European approach to business failure and insolvency [2012] OJ C 271/ 55.
[17] Commission Recommendation C(2014) 1500 final of 12 March 2014 on a new approach to business failure and insolvency [2014] OJ L 74/65 (the "Recommendation").

States.[18] The objective of the Commission, according to the Recommendation, was to "ensure that viable enterprises in financial difficulties…have access to national insolvency frameworks, which enable them to restructure at an early stage with a view to preventing their insolvency…"[19] It was argued that preventing insolvency would maximise the value to the economy as a whole, benefit those connected with businesses at risk of insolvency, such as creditors, employees and owners, and contribute to saving jobs.[20] The Commission also sought to give honest bankrupt entrepreneurs a "second chance", which it viewed as potentially increasing self-employment rates in Member States, amongst other benefits.[21] Variances in both how Member States treated restructuring and the national rules on a second chance for honest entrepreneurs led to a reluctance on the part of businesses to expand across the European Union, either by virtue of the increased costs or uncertainty as to their level of exposure in other Member States, and very different recovery rates for creditors.[22] As such, the Commission believed that:

> "the creation of a level playing field in these areas would lead to greater confidence in the systems of other Member States for companies, entrepreneurs and private individuals, and improve access to credit and encourage investment."[23]

The Recommendation noted that SMEs, in particular, would benefit from the Recommendation as paying high restructuring costs was not feasible for such companies, something which reflected the position taken by the Commission in 2012 in its Communication to the Parliament.[24]

Key to the Recommendation of the Commission were the following points:

- Flexibility of procedures, namely limiting the need for court formalities to where they are necessary and proportionate;[25]
- Provision for a stay of individual enforcement actions;[26]
- Protection of the interests of dissenting creditors, namely that the court should reject any restructuring plan which would likely reduce the rights of dissenting creditors below what they could reasonably expect to receive, were the debtor's business not restructured;[27] and
- Provision for "second chance", namely that provisions should be made for a full discharge of debt after a specified period of time.[28]

Part I of the Recommendation lays out its objectives, namely to encourage Member States to establish efficient restructuring frameworks, which it was submitted would, in turn, promote entrepreneurship, investment and employment and reduce "obstacles to the smooth functioning of the internal market."[29] The aims of the Recommendation are also contained in Part I and are to lower the costs of assessing risks of investing in other Member States; to increase recovery rates for creditors; and to remove difficulties in restructuring cross-border groups of companies, respectively.[30]

[18] Commission, 'Impact Assessment Accompanying the document Commission Recommendation on a New Approach to Business Failure and Insolvency' [2014] (Staff Working Document) SWD (2014) 61 final 1 ("Impact Assessment of Recommendation").
[19] Recommendation, recital 1.
[20] Recommendation, recital 1 & 12.
[21] *ibid*.
[22] *idem* recital 4.
[23] *idem* recital 8.
[24] *idem* recital 13.
[25] *idem* recital 17.
[26] *idem* recital 18; the recommendation was that the stay should be available for a period of no more than four months initially, in order to balance the rights of creditors.
[27] Recommendation, recital 19.
[28] *idem*, recital 20; it was felt that this particular aim would help to combat the "social stigma" and legal consequences of an on-going inability to pay off debts. Part IV of the Recommendation concerns "second chance" provisions; the Commission recommended that entrepreneurs should be fully discharged of their debts within three years from either the date on which implementation of a payment plan began or the date on which the court approved the opening of bankruptcy proceedings (section 30). Per s 32, however, Member States are entitled to introduce more stringent provisions in certain circumstances, for example to discourage entrepreneurs who have acted in bad faith or failed to adhere to a repayment plan, or to safeguard the livelihood of the entrepreneur by allowing him / her to keep certain assets.
[29] Recommendation, s 1.
[30] *ibid*.

Part III of the Recommendation set out the Commission's position on preventative restructuring frameworks, which covered a number of areas. Section 6 lists common principles or elements which should be part of all national insolvency frameworks, namely:

(i) the availability of early restructuring for debtors likely to become insolvent;

(ii) the debtor retaining control over the day-to-day business operations;

(iii) the availability of a stay of individual enforcement action;

(iv) cram-down; and

(v) protection for new financing.[31]

Sections 7 through 9 reflect the intention laid out in recital 17, namely that Member States should adopt a less rigid approach to insolvency proceedings by confining the involvement of national courts to where such involvement is necessary and proportionate; by ensuring that debtors need not formally open court proceedings in order to begin the process of restructuring their business; and by ensuring that the appointment of a mediator or supervisor be done on a case by case basis, as opposed to being mandatory.[32]

The importance placed by the Commission on the stay of individual enforcement actions is highlighted in sections 10 through 14. It is recommended that debtors should have the right to request a stay where individual actions may hamper the restructuring process.[33] A stay should be granted in all circumstances where there is widespread, though not necessarily universal, support amongst creditors for the process and the plan has both a reasonable prospect of being implemented and of preventing the insolvency of the debtor.[34] The Commission also seeks to strike a balance between the rights of debtors and creditors by limiting the duration of the initial stay to 4 months and the total duration (with extensions) to 12 months.

Section 18 of the Recommendation provides for the introduction (or retention) of provisions which empower courts to confirm restructuring plans that are supported by the majority of classes of creditors, once due regard is given to the claims of the respective classes of creditors, i.e. cross-class cram-down. Sections 21 through 23 set out the approach that Member States should adopt in relation to court confirmation of restructuring plans, with section 22 stating that the law on court confirmations should be clear. It sets minimum requirements, including that the restructuring plan does not reduce the rights of dissenting creditors below what they would reasonably be expected to receive in the absence of restructuring and that any new financing is both necessary and does not unfairly prejudice the interest of dissenting creditors.[35] Section 26 recommends that court approved restructuring plans should be binding upon every affected creditor, in other words "cram-down".

Finally, sections 27 through 29 deal with protection for new financing during the restructuring process; the Commission recommends that new financing, contained in the agreed restructuring plans and approved by a court, should not be declared void as an act detrimental to the general body of creditors and that in the absence of any justified exception to the rules protecting new finance, providers of new financing should be exempt from civil and criminal liability relating to the restructuring process.[36]

The Impact Assessment accompanying the Recommendation[37] identified three general policy objectives of the Recommendation, namely to contribute to the smooth functioning of the internal market by enabling restructuring of viable businesses (and liquidation of unviable ones); to enhance the survival prospects of firms in difficulty; and to minimise investment decisions being made on foot of national insolvency laws.[38] The Impact Assessment also identified a number of specific objectives, including to

[31] *idem* s 6.
[32] *idem* ss 7-9.
[33] *idem* s 10.
[34] *idem* s 11; this section applies to Member States which impose certain conditions on the granting of a stay.
[35] Recommendation, s 22 (c)(d).
[36] *idem* ss 27-29.
[37] Impact Assessment of Recommendation.
[38] *idem* 26.

reduce the cost of restructuring in Member States with inefficient rescue processes and reduce the cost to creditors resulting from the relocation of debtors.[39] The Impact Assessment also identified two viable policy options for the Recommendation: a Commission recommendation to Member States or a Directive. Both would aim to deal with introducing minimum standards for preventative restructuring frameworks and second chance.[40]

The Commission considered the first policy option of maintaining the status quo and the fourth of a fully harmonised procedure to be unsuitable, as they would, respectively, fail to achieve the objectives set out by the Commission and would be a disproportionate response to the issues identified. Within sub-options 2 and 3, the Impact Assessment identified a number of sub-options.[41] For the purposes of this Report, the sub-options under the stay or moratorium, protection of new financing, plan approval by a majority of creditors (cram-down), and less court formality within preventative restructuring will be analysed.

a) The Stay

The sub-options laid out under the moratorium were that:

1. a stay would be granted automatically against all creditors;
2. a stay would be granted at the request of the debtor;
3. a stay of short, limited duration would be granted at the request of the debtor.

In the analysis of the impacts of the policy options for the stay, sub-option (3) was considered to be the most appealing as it was felt that it struck the best balance between the interests of all parties involved. A stay of limited duration was viewed to reduce the length of the restructuring procedure, thereby limiting the detriment caused to creditors, but also providing for the possibility of extension in certain circumstances.[42] What is interesting to note about sub-options (2) and (3) is that both referred to a stay *at the request of the debtor* and under sub-option (2) it was noted that countries such as Ireland, which has an "automatic stay in place", would need to provide for a stay on request.[43] In contrast, the PRD, which will be discussed in more detail later in this Report, only provides for the existence of a stay for the benefit of debtors. It does not specify that the stay must be at the request of the debtor, thereby seeming to contradict the link between the sub-option and the benefit to the effectiveness of the procedure identified by the Impact Assessment.[44]

b) Protection of New Financing

Two sub-options were provided under the heading of new financing,[45] namely:

1. Super-priority status for new financiers;
2. Exempting approved new financing from avoidance actions except in the case of fraud. Member States may also grant super-priority status.

Sub-option (2) was considered to be the preferable option as it was contended that it provided "the necessary incentives and support for restructuring plans to be successful, without unduly affecting the

[39] *idem* – see table of specific objectives.
[40] *idem* 27.
[41] *idem* see table of sub-options for Options 2 and 3, 27-28.
[42] *idem* 30-32.
[43] *ibid*; Arguably, to state that Ireland has an "automatic stay in place" was somewhat misleading, rather the Irish legal position is that a company receives court protection for a limited duration on foot of the presentation of a petition for the appointment of an examiner by the relevant court. As a petitioner the debtor can initiate the process applying for the appointment of an examiner and hence the commencement of the stay. Other potential petitioners include creditors, employees or contributories. In all cases the stay will be imposed pending the hearing but will be lifted in the petition to grant an examiner is not granted or is subsequently denied following a full hearing.
[44] See Impact Assessment of Recommendation 30: "The stay should be on request by the debtor, so that debtors who are able to continue to pay their debts as they fall due and do not need a stay can negotiate in confidentiality with those creditors which they need to involve."
[45] Impact Assessment of Recommendation 30.

rights of existing creditors."[46] It was felt that where the rights of creditors were impacted, these were proportionate if the alternative was to be the liquidation of the debtor.[47]

c) Cram-Down

Three sub-options were identified under the heading 'Plan approval by a majority of creditors':[48]

1. A majority of creditors could be bound by a majority in the same class, but Member States may exclude secured creditors from majority voting;

2. A minority of creditors in any class could be bound by a majority of creditors in the same class, with decisions made by formal voting;

3. A minority of creditors in any class could be bound by a majority of creditors in the same class without the need for a formal voting process, provided the debtor can prove the majority support.

Sub-option (3) was considered preferable, as it was opined that it would ensure that secured creditors could also be bound by the plan, thereby promoting greater likelihood that a restructuring process would succeed, as secured creditors are critical to the restructuring process.[49] Furthermore, it was the position of the Impact Assessment that such a policy would increase efficiency by reducing the time and cost with organising formal voting but not at the expense of proper oversight. As is evident, the option did not outline a mechanism for cross-class cram-down; instead, it merely gave scope for Member States to make provisions for cram-down (majority rule within classes) in the concluding paragraph. Interestingly as was noted earlier, section 18 of the Recommendation does provide for cross-class cram-down, which it could be argued results in some inconsistency between the two related documents. Article 11 of the Directive also includes a provision for cross-class cram-down, thus it is seemingly more in line with the Recommendation.

d) Decreased Formality

Two sub-options were provided under the heading 'Reducing the formalities relating to court proceedings': [50]

1. A flexible framework, providing for more limited court involvement save in certain circumstances (e.g. it is necessary to prevent abuse);

2. A flexible framework, providing for more limited court involvement save in certain circumstances, but which requires courts to rule in principle in written procedure.

The position of the Impact Assessment was that sub-option (2) was the most suitable as it balanced the need to reduce costs of restructuring with protecting the procedural right of parties. It is interesting to note the view in the Impact Assessment that Member States, such as Ireland and the Netherlands, would need to "make possible that courts are not seised when negotiations start, but at a later stage when the prospects of a restructuring plan are also more tangible."[51]

5.2.4 Conclusion

The response of the Member States to the Recommendation and accompanying Impact Assessment was lacklustre. An evaluation of the Recommendation was carried out by the Directorate-General Justice &

[46] *idem* 37; It should be noted that as part of its analysis, the Commission commented on the impact that granting super-priority to new finance would have on the property rights of some creditors. The Impact Assessment noted that the granting of super-priority to new finance may lead to a limitation in the exercise of the right to property of dissenting creditors.
[47] Impact Assessment of Recommendation 37.
[48] *idem* 28.
[49] *idem* 35.
[50] *idem* 28.
[51] *idem* 38. As will be evident upon discussing the final wording of the PRD, Ireland and other Member States with similar provisions are unlikely to have to make changes to national law.

Consumers of the European Commission in 2015,[52] with 24 countries from 28 taking part. There are two points worth making in relation to this Evaluation; the first relates to the language utilised and the second relates to the findings.

First, the language employed in the Evaluation is quite vague; in Part 1, it was noted that "a few Member States [had] undertaken reforms which, in some cases, resulted in legislation implementing the Commission's Recommendation".[53] Although examples of such Member States were provided in Part 1, it was noted that "in most cases" the legislation only partially implemented the Recommendation.[54] One could contend that language such as "a few", "in some cases" and "in most cases" lacks the specificity and analytical quality that one would expect from an evaluation, particularly one where the goal was to assess the impact of a Commission Recommendation. Instead, it is submitted that the Evaluation tends more towards being a discussion of the position of the respondents on some aspects of insolvency law.

The Evaluation does give some insight into the ways in which Member States were partially compliant with the Recommendation, somewhat mitigating against the vagueness in Part 1. With that said, however, the analysis of the legal position in the Member States only served to highlight their lack of engagement. Consider the stay, for example, as was highlighted earlier the Recommendation advocated for the availability of a stay of short, limited duration at the request of the debtor. Yet at the time of the Evaluation, there was no possibility of a stay in Austria and a number of countries, including Romania and Belgium, provided for a stay of indefinite length.[55] On the matter of protection for new financing, the Recommendation advocated for approved new financing being exempt from avoidance actions except in the case of fraud and for the option for Member States to grant super-priority status. At the time of the Evaluation, a number of Member States including Luxembourg and Sweden offered no special protection to new financiers in subsequent insolvency proceedings.[56] Furthermore, in both examples, some of the responding Member States were absent from analysis.

Following on from the lack of legislative activity among the Member States following its Recommendation, the Commission established the Expert Group on Restructuring and Insolvency Law, which met a number of times throughout 2016. It was comprised of over 20 leading academics and practitioners from 12 EU countries and its function was to discuss various aspects of insolvency law and more specifically, to focus on how the Commission Recommendation could be amended, thereby making it more effective across the EU and leading to more legal certainty.[57] A full discussion of the meetings of the Expert Group is contained in Annex 1 of this Report. However, one aspect of discussion around the stay was particularly relevant for the purposes of this Report. Some of the experts had "strong concerns" that the stay would be open to abuse and they referred to the "moral hazard problem" on more than one occasion.[58] There was clear divergence between the experts as to whether the stay should be automatic and general. Those experts who expressed concern regarding abuse stated that the stay should be neither automatic nor general, whereas other members were of the view that the stay should be automatic at first, otherwise it would be "cumbersome for a court to determine if there are reasonable prospects of success of the restructuring".[59] The reference to the moral hazard problem is interesting, as it highlights, once again, how differing traditions and cultures lead to very different opinions on how the law should function.

5.3 The Commission Proposal

In November 2016 the Commission issued its Proposal for a Directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU. One of the main justifications given by the

[52] Directorate-General Justice & Consumers of the European Commission, 'Evaluation of the implementation of the Commission Recommendation of 12.3.2014 on A New Approach to Business Failure and Insolvency' (2015.

[53] *idem* 1.

[54] *ibid.*

[55] *idem* 3.

[56] *idem* 4.

[57] Minutes Expert Group Meeting – 14 January 2016 3: "[t]he view shared by the majority of the experts is to focus on how the Insolvency Recommendation may be improved as to provide more legal certainty and more binding force in Member States."

[58] Broadly speaking, moral hazard occurs when a party takes increased risks because they are aware that another party will bears the cost of those risks. See Minutes Expert Group Meeting 14 June 2016, 3 and Minutes Expert Group Meeting 11 July 2016, 3.

[59] Minutes Expert Group Meeting 14 June 2016, 3-4.

Commission for proposed directive was similar to the justification given for the Recommendation circa four years previously. Uncertainty regarding local insolvency rules and/or the risk of a complex and costly restructuring as a result of national systems were the primary reason for the reluctance of investors to expand outside their own country.[60] It was the view of the Commission that:

> "[a] higher degree of harmonisation in insolvency law is thus essential for a well-functioning single market and for a true Capital Markets Union" as "increased convergence of insolvency and restructuring procedures would facilitate greater legal certainty for cross-border investors and encourage the timely restructuring of viable companies in financial distress".[61]

5.3.1 The Stay

Article 6 and 7 of the Commission Proposal pertained to the stay, with the latter detailing the consequences of a stay of individual enforcement and the former giving the mechanics of the provision. Article 6(1) stated:

> "Member States shall ensure that debtors who are negotiating a restructuring plan with their creditors may benefit from a stay of individual enforcement actions if and to the extent that such a stay is necessary to support the negotiations of a restructuring plan."

Article 6(2) provided for the stay to extend to all types of creditors and to be general in nature or limited to particular creditors.[62] Articles 6(4)-6(7) pertain to the duration of the stay; article 6(4) placed a maximum time limit of four months on the (initial) stay and 6(5) granted Member States the ability to provide for extensions, or the granting of a new stay, if the negotiations were progressing and the extension was not unfairly prejudicial.[63] 6(7) placed a time limit of 12 months on the total duration of the stay, including extensions and renewals. Articles 6(8) and 6(9), respectively, outlined the conditions for the lifting of the stay by a judicial or administrative authority and mandated Member States to provide for the judicial or administrative authority refusing or lifting the stay at the request of creditors unfairly prejudiced by the stay.

Article 7(1) and 7(2) apply to insolvency proceedings with the former stating that any obligation to file for insolvency under national law is suspended for the duration of the stay and the latter dictating that a general stay prevents the opening of insolvency procedures at the creditors' request.[64] Article 7(4) specified that Member States should prevent affected creditors from withholding performance or terminating or modifying executory contracts to the detriment of the debtor for debts occurring prior to the stay.[65] Article 7(5) specified that Member States should prevent creditors from withholding performance or terminating or modifying executory contracts solely by reason of the debtor's entry into restructuring negotiations, a request for a stay, the ordering of the stay, or any similar event connected to the stay.[66] Article 7(6) dictated that Member States must ensure that debtors are not precluded from paying certain claims, namely those of creditors unaffected by the stay and those that arise after the stay is granted and reoccur throughout the stay. Lastly, article 7(7) stated that Member States should ensure that debtors are not required to file for insolvency procedures if the conditions laid down by national law are met, not solely because the stay period has expired without a plan agreed.

[60] Proposal, 2.
[61] Proposal, 2.
[62] Proposal, art 6(3) excluded workers' claims from the scope of s 6(2) except where Member States ensure that the claims are protected to the same extent as they would be under the national interpretation of 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 [2008] OJ L 283/36.
[63] Proposal, art 6(6) adds an additional condition to the granting of an extension, namely the "strong likelihood" that the plan will be adopted.
[64] Proposal, art 7(3) provides an exception to art 7(1) as follows: "[w]here the debtor becomes illiquid and therefore unable to pay his debts as they fall due during the stay period … Member States shall ensure that restructuring procedures are not automatically terminated and that, upon examining the prospects for achieving an agreement on a successful restructuring plan within the period of the stay, a judicial or administrative authority may decide to defer the opening of insolvency procedure and keep in place the benefit of the stay of individual enforcement actions."
[65] Proposal, art 7(4) went on to state; "Member States may limit the application of this provision to essential contracts which are necessary for the continuation of the day-to-day operation of the business."
[66] There is currently a variety of approaches among Member States in relation to these so-called *ipso facto* clauses. See Jason Chuah and Eugenio Vaccari (eds), *Executory Contracts in Insolvency Law* (Elgar 2019) for a detailed discussion on this topic.

5.3.2 Protection for New Finance

Article 16 pertained to the protection of new finance. Article 16(1) stipulated that new and interim finance should be "adequately encouraged" and specifically, that it should not be declared void or unenforceable in subsequent insolvency proceedings, unless other criteria were met.[67] Article 16(2) mandated that new or interim financiers should be ranked senior to unsecured creditors. Furthermore, it stated that Member States may decide to grant priority status to new and interim finance in subsequent insolvency proceedings. Finally, article 16(3) absolved new and interim financiers from criminal and civil liability in subsequent insolvency proceedings unless the transactions were fraudulent or carried out in bad faith.

5.3.3 Cross-Class Cram-Down

Article 11 of the Commission Proposal related to cross-class cram-down, with article 11(1) providing for a restructuring plan to be binding on dissenting creditors once it was approved by a judicial or administrative authority and complied with three criteria:

a) Compliance with article 10(2);[68]

b) Approval of at least one class of affected creditors[69] and any other class, which would not receive any payment if liquidation occurred; and

c) Compliance with the absolute priority rule.

Article 11(2) gave Member States latitude to decide the number of affected classes which would be required to approve the restructuring plan in order to cram-down on dissenting creditors.

5.3.4 Decreased Court Formality

Article 4(3) applied to decreased formality within restructuring processes. It stated:

> "Member States shall put in place provisions limiting the involvement of a judicial or administrative authority to where it is necessary and proportionate so that rights of any affected parties are safeguarded."

5.4 The Consultation Process

Throughout 2017 and 2018, various bodies expressed opinions and, in some cases, suggested specific amendments to the proposal. Broadly speaking, these submissions are considered chronologically, however, some bodies, such as the Council via the Justice and Home Affairs Council, held a number of debates throughout the aforementioned time period.[70] As will become evident, the Council had the greatest impact on the content of the final Directive and as such, its amendments are discussed in considerably more detail than the amendments proposed by other various committees, such as the European Economic and Social Committee and the European Parliament Committee on Employment and Social Affairs. It would seem that much of the impact of amendments from these committees seemed to be increasing the degree to which workers were referenced in the final text. One key aspect to take away from the consultation process was the considerable weakening of the provision mandating the decrease in court formality, something which was supported by a number of parties to the consultation process.

[67] Fraudulent transactions or those carried out in bad faith.

[68] Proposal, art 10(2) stated; Member States shall ensure that the conditions under which a restructuring plan can be confirmed by a judicial or administrative authority are clearly specified and include at least the following: (a) the restructuring plan has been adopted in accordance with art 9 and has been notified to all known creditors likely to be affected by it; (b) the restructuring plan complies with the best interest of creditors test; (c) any new financing is necessary to implement the restructuring plan and does not unfairly prejudice the interests of creditors.

[69] Aside from equity-holders.

[70] In the interest of expediency, a number of bodies / committees which commented on and/or proposed amendments to the Commission Proposal have been removed from the main body of the Chapter. A fuller discussion of those submissions is available in Annex 1 of this Report. These submissions are: the opinions of the national parliaments (Annex 1, para 10.6.2) and the opinion from the Committee of the Regions (Annex 1, para 10.6.5).

5.4.1 European Economic and Social Committee[71]

In early 2017, mandatory consultation with the European Economic and Social Committee (henceforth "the EESC") took place. In general, the Committee expressed support for the proposal, in particular, noting its preference that the EU not be afraid to move towards the maximum possible harmonisation. The Committee did, however, seem to have concerns regarding the degree to which the proposal protected the rights of workers. As such, most of its recommendations pertained to worker protection. However, there are some points to note in relation to decreased court formality and the stay, which are outlined below.[72]

The Committee strongly supported the "marginal role granted to the courts" at point 1.10 of the EESC Opinion and supported limiting the role of the courts to "intervene only in cases of necessity" in the insolvency process. At point 1.7 the Committee contended that members of the judiciary should have "appropriate common training and extensive experience" which would enable them to work in this area.[73] This is reflective of the concerns of members of the judiciary that have been expressed in JCOERE several meetings. Furthermore at point 4.2.8 of the EESC Opinion, it was noted that the objective was "to reduce action taken by judicial / administrative authorities" which, in the view of the EESC, were too frequently called upon prematurely "to solve insolvency issues using drastic measures."[74] Regarding the stay, the Committee advocated for abuse of the insolvency process (the "tactical use of insolvency procedures to avoid legal liability and deny workers their rights") to be an illegal practice, which critically, they argued, should render a stay unattainable.[75]

5.4.2 The European Central Bank[76]

In mid-2017, the European Central Bank issued its opinion on the proposal; while the ECB broadly welcomed the proposed directive, it did express reservations in relation to certain aspects. In stark contrast to the Member States, the ECB lamented the lack of harmonisation in what it considered to be key areas of insolvency law such as a definition of insolvency, the conditions for opening insolvency proceedings, the ranking of insolvency claims and avoidance actions and cited the need for "more

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[71] European Economic and Social Committee, 'Opinion: Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU' (Business Insolvency) INT/810 ("EESC Opinion").

[72] For example, at point 1.5 of the EESC Opinion, the Committee recommended that workers attain the status of priority creditors in all Member States and that employees and unions must be involved throughout the process including having the ability to make alternate proposals and refer an expert (point 4.2.4). At point 1.3 of the EESC Opinion, the EESC insisted that the final text;
provide for mandatory consultation by company management with employees prior to and during the negotiation process,
give greater importance to workers' interests early in the restructuring process, and
make specific reference to Article 5(2) of Directive 2001/23 to protect the rights of workers.
It is worth noting that there is an error in the Committee opinion, as point 1.3 actually advocates for reference to be made to "Article 5(2) of Directive 2011/23" The correct Directive is 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 OJ L 82/16, art 5(2) of which reads:

> "Where Articles 3 and 4 apply to a transfer during insolvency proceedings which have been opened in relation to a transferor (whether or not those proceedings have been instituted 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 practitioner determined by national law) a Member State may provide that:
>
> (a) notwithstanding art 3(1), 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, under the law of that Member State, to protection at least equivalent to that provided for in situations covered by Council Directive 80/987/EEC of 20 October 1980 on the approximation of the laws of the Member States relating to the protection of employees in the event of the insolvency of their employer(7), and, or alternatively, that,
>
> (b) the transferee, transferor or person or persons exercising the transferor's functions, on the one hand, and the representatives of the employees on the other hand may agree alterations, in so far as current law or practice permits, to the employees' terms and conditions of employment designed to safeguard employment opportunities by ensuring the survival of the undertaking, business or part of the undertaking or business."

[73] At 4.5.1 of the EESC Opinion, the Committee stated that it would be helpful if the aforementioned training was "organised directly be the Commission (including through agencies)".

[74] The JCOERE 2 Report will return to this issue, along with the role of the judiciary/ administrative authority envisaged in art 11 of the Directive regarding confirmation of plans which include cross-class cram-down.

[75] EESC Opinion points 4.2.3 & 1.9.

[76] European Central Bank 'Opinion on a proposal for a directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU' (Communication) CON/2017/22 OJ C 236/02 ("ECB Opinion").

ambitious action" to be taken.[77] In relation to the stay, in particular, the ECB expressed concern about the unintended consequences of the directive.[78] At para 1.7 it was noted that:

> "…the consequences and scope of the stay, such as whether the stay of individual enforcement actions also applies to assets of the debtor pledged as collateral for claims of the creditor, need to be carefully assessed also from the perspective of its possible impact on regulatory capital requirements, and in particular from the perspective of risk mitigation techniques under Regulation (EU) No 575/2013 of the European Parliament and of the Council."[79]

No attempt was made to further harmonise the aforementioned areas in light of the opinion of the ECB. As such, one could opine that perhaps the "considerable legal and practical challenges" associated with further harmonisation, as identified by the ECB in its Opinion, were considered too great by the Parliament and Council.

5.4.3 European Parliament Committees: Committee on Legal Affairs[80]

The Committee on Legal Affairs issued an extensive report on the Commission proposal in September 2017. The Committee suggested a significant number of amendments to the proposal, 85 in total and demonstrated a tendency towards more conservativism in its approach to issues such as the stay and decreased court formality.[81]

a) The Stay

Amendments 39 to 51 applied to articles 6 and 7. At Amendment 39, the Committee proposed attaching the conditions that the "obligation of the debtor to file for insolvency under national law" had not yet arisen and that there was a likelihood of being able to save the company from insolvency to the availability of the stay under article 6(1).[82] At Amendment 40, the Committee attempted to limit the stay to only those creditors that were "participating in the negotiation of a restructuring plan"[83] Arguably, however, creditors who are not participating in the negotiation process could be the most likely creditors to initiate proceedings against the debtor, if it appears as though they may be disadvantaged by the process. Interestingly, the Committee also attempted to reduce the maximum duration of the stay from four months to two and the total duration of the stay including extensions from twelve months to six via Amendments 41 and 46.[84] Furthermore, the Committee also attempted to insert the following after article 6(7):

> "The total duration shall be limited to two months if the registered office of the company has been transferred to another Member State within a three-month period prior to the filing of a request for the opening of restructuring proceeding."

[77] ECB Opinion para 1.2.
[78] Essentially, the ECB was concerned that financial institutions may suffer unintended consequences as a result of the impact that the stay may have on financial contracts with commercial entities.
[79] ECB Opinion para 3.
[80] European Parliament Committee on Legal Affairs, Report of 22 September 2017 on the proposal for a directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU COM(2016)0723 – C8-0475/2016 – 2016/0359(COD) ("Report by Committee on Legal Affairs").
[81] The Committee on Legal Affairs proposed no amendments to the protection of new financing. The amendments proposed to cross-class cram-down were not included in the final draft. The Committee advocated for the amendment of article 11(1)(b) to require that the restructuring plan be approved by "the majority of classes of affected creditors," as distinct from "at least one class of affected creditors" contained in the proposal. The Committee proposed amending article 11(2) as follows: "Member States may vary the minimum number of affected classes required to approve the plan laid down in point (b) of paragraph (1) to the extent that that minimum number covers still the majority of classes."
[82] Report by Committee on Legal Affairs 29. The Committee also sought to amend art 6(5) – conditions for granting an extension to the stay – to include the same condition, namely that the obligation of the debtor to file for insolvency under national law had not yet arisen.
[83] Report by Committee on Legal Affairs 29.
[84] Report by Committee on Legal Affairs 30 & 32.

It appears that none of the amendments that the Committee put forward in relation to article 6, were adopted. The Committee also proposed a number of changes to article 7[85] but it appears, however, that none of these were integrated into the final draft either.[86]

b) Decreased Court Formality

The Committee sought to weaken to position of the Commission on decreased court formality by replacing the word "shall" with "may" in article 4(3);[87] as such, the requirement for Member States to put provisions in place to limit formality to where it was necessary and proportionate was no longer present. This is one area where the position of the Committee was reflected in the final text of the PRD, as the word "may" remained in article 4(6).[88]

5.4.4 European Parliament Committees: Employment and Social Affairs ("EMPL")[89]

In December 2017, the European Parliament Committees on Employment and Social Affairs and on Economic and Monetary Affairs issued opinions on the Proposal. The EMPL opinion mirrored much of the concern expressed by the EESC earlier in the same year, namely that workers had not been adequately considered in the proposed directive. As such, the Committee went on to suggest a number of changes to the proposed text. Amendments 1 – 24 proposed by the EMPL Committee, were to the recitals of the Proposal, suggesting either the insertion of a new recital or the amendment of an existing one. Amendments 25 – 64 applied to articles of the Proposal, all with a view to strengthening the position of workers.[90]

Although many of the EMPL Committee proposals were not specifically adopted by the Parliament, the revised article 8(1)(g) includes a specific reference to the arrangements for informing and consulting the employees' representatives and the overall consequences for employees e.g. dismissals, changes to working arrangements. Arguably, this indicates that the canvassing for greater protection of employees carried out by various parties did have some impact on the final wording of the PRD.

In the following section, this Report will consider the amendments proposed by the EMPL Committee to the key areas relevant to this report, namely the stay and protection of new finance. The proposed amendments pertaining to decreasing court involvement in insolvency matters were quite minor and there were no amendments proposed to cross-class cram-down.[91]

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[85] Amendments 47 – 51 applied to art 7 of the Proposal and again, one could argue that that there was evidence of a tendency towards conservatism. The Committee on Legal Affairs advised amending art 7(1) to provide that the stay not apply in situations where the debtor was obliged to file for insolvency under national law and proposed deleting art 7(2), which limited the right of creditors' to open insolvency proceedings during the stay, See the Report by Committee of Legal Affairs 32. The Committee also proposed deleting art 7(3):

> "Member States may derogate from paragraph 1 where the debtor becomes … unable to pay his debts as they fall due during the stay period. In that case, Member States shall ensure that restructuring procedures are not automatically terminated and that, upon examining the prospects for achieving an agreement on a successful restructuring plan within the period of the stay, a judicial or administrative authority may decide to … keep in place the benefit of the stay...".

The Committee also proposed deleting art 7(6): "Member States shall ensure that nothing prevents the debtor from paying in the ordinary course of business claims of or owed to unaffected creditors and the claims of affected creditors that arise after the stay is granted and which continue to arise throughout the period of the stay."

[86] Article 7(6) was removed, but the wording features in recital 39 of the PRD instead. Article 7(4) was reworded once more before the final text, so neither the Committee recommendations nor the original proposal text remained. The other amendments, 47-49, were not accepted.

[87] Committee on Legal Affairs Opinion p. 26.

[88] Article 4(6); "Member States may put in place provisions limiting the involvement of a judicial or administrative authority in a preventive restructuring framework to where it is necessary and proportionate while ensuring that rights of any affected parties and relevant stakeholders are safeguarded."

[89] European Parliament Committee on Employment and Social Affairs, Opinion of 5 December 2017 on the proposal for a directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU COM(2016)0723 – C8-0475/2016 – 2016/0359(COD) ("Opinion of EMPL Committee").

[90] See Annex 1 for a more thorough discussion of the amendments relating to workers' rights.

[91] The is worth noting that the EMPL Committee proposed amendments to cram-down, as opposed to cross-class cram-down in Amendments 45 through to 48. Generally speaking, the proposed amendments were to provide for further protection of workers; for example, the amendment of art 9(4) added "the workers class" after the reference to "each and every class", a proposal that was not adopted by the Parliament. It was also suggested that art 9(1) be amended to specifically include workers in the creditors that should have the right to vote on the adoption of a restructuring plan and including the caveat that parties must be "duly informed about the procedure and its potential consequences for the company". The original art 9(1) read: "Member States shall ensure that any affected creditors have a right to vote on the adoption of a restructuring plan." The amendment read: "Member States shall ensure that the procedures provided for in national law allow creditors, including workers affected by a waiver plan, to have a right to vote on the adoption of the restructuring plan, after having been duly informed about the procedure and its potential consequences for the company." The Committee also proposed amending art 9(2) to state, in much stronger terms, that workers should have a privileged position by replacing "Member States may also provide that workers are treated in a

a) The Stay

Few amendments proposed by EMPL applied to the stay of individual enforcement.[92] The Committee did, however, propose one interesting amendment in that it advocated for employees to be specifically excluded from the types of creditors who could be affected by a stay of individual enforcement:

> "Member States shall ensure that a stay of individual enforcement actions may be ordered in respect of all types of creditors, including secured and preferential creditors **but excluding workers**."

In justifying this change, the Committee acknowledged the protection for workers contained in article 6.3; however, it was their view that workers needed to be expressly excluded.[93]

b) Protection of New Financing

The Committee sought to reduce the protection afforded to new finance by removing article 16(2) from the proposed directive. The justification the Committee offered was their belief that it constituted "a super-privilege for actors providing new and interim financing", which it was argued could result in "downgrading of other creditors including workers", thereby reducing the "remaining substance of the concerned enterprise, thereby further endangering workers". Despite the concerns expressed by the Committee, article 17(4) of the Directive gives Member States the ability to treat the providers of new or interim financing with priority in the context of subsequent insolvency procedures.

5.4.5 European Parliament Committees: Economic and Monetary Affairs ("ECON")[94]

Broadly speaking, the changes proposed by the Committee on Economic and Monetary Affairs focused on strengthening the position of smaller entrepreneurs, vulnerable creditors and workers and occasionally on providing for more assurances that restructuring processes would be successful.[95] The ECON Committee Opinion embodied an attempt towards balancing competing interests with successful restructuring, particularly in the areas of focus of this report. The bulk of the relevant amendments applied to the stay; as such, it and decreased court formality are discussed below.[96]

a) Stay

Amendments 51 – 56 pertained to article 6 of the proposal. The Committee wished to amend article 6(1) to mandate Member States to specify "[p]articular conditions … in order to ensure that such a stay is necessary" and advocated for mandating Member States to require that debtors benefiting from a stay were "viable".[97] The proposed amendment to article 6(2) attempted to make it a condition of limited stays rather than general and to ensure that they do not "endanger the efficiency and success of the restructuring plan".[98] The focus of the Committee on balancing the rights of affected parties with ensuring that the success of the restructuring process was evident in amendments such as this. In Amendment 53, the Committee attempted to exclude the claims of "micro and small enterprises" in

separate class of their own" with "Taking into account that workers are a class of preferential creditors, except in duly justified circumstances, Member States shall also ensure that outstanding wage claims for active workers and pension claims for retired workers are treated in a separate preferential class of their own, and shall guarantee the priority of such claims" The original wording of the article, now art 9(4), was retained, however.

[92] The EMPL Committee did propose removing the phrase "in principle" from recital 34, thereby changing it to "Given the need to ensure an appropriate level of protection of workers, Member States should exempt workers' outstanding claims …from any stay of enforcement irrespective of the question whether these claims arise before or after the stay is granted."

[93] The proposed art 6(3) stated: "Paragraph 2 shall not apply to workers' outstanding claims except if and to the extent that Member States ensure by other means that the payment of such claims is guaranteed at a level of protection at least equivalent to that provided for under the relevant national law transposing Directive 2008/94/EC."

[94] European Parliament Committee on Economic and Monetary Affairs, Opinion of 7 December 2012 on the proposal for a directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU COM(2016)0723 – C8-0475/2016 – 2016/0359(COD) ("ECON Committee Opinion").

[95] See, as discussed later, the inclusion of a requirement that Member States require that debtors benefiting from a stay are "viable".

[96] For the sake of efficiency, the minor amendment to art 17 (protection of new finance) and the amendments to cram-down are discussed in Annex 1.

[97] ECON Committee Opinion 32.

[98] Originally, art 6(2) read; Member States shall ensure that a stay … may be ordered in respect of all types of creditors, including secured and preferential creditors. The stay may be general … or limited, covering one or more individual creditors, in accordance with national law".

addition to workers' claims from being covered by the stay.[99] In Amendments 54 and 55, the ECON Committee attempted to reduce the duration of the initial stay to between 3 and 6 months and the maximum duration, including extensions, to 9 months.[100] It is curious that the Committee would, on the one hand, seek to increase the maximum duration of the (initial) stay while, on the other hand, attempting to decrease the maximum duration, including extensions. In any event, neither of the proposed changes to the duration of the stay, or indeed the other changes proposed by the ECON Committee, were accepted for the final text. The final amendment sought by the ECON Committee to article 6 was the specific inclusion in article 6(9) of the suffering of financial difficulties by a "vulnerable creditor" as a justification for the stay being lifted or refused by the judicial or administrative authority and the statement that "[a]n unfair prejudice shall be deemed to exist at least where a creditor or class of creditors is facing considerable economic difficulties."[101] As was the case with the other amendments to article 6, they were not incorporated.[102]

b) Decreased Court Formality

The ECON Committee Opinion suggested amending article 4(3) to replace "shall" with "may", thereby making it optional for Member States to limit judicial involvement. As was noted earlier, the final wording of article 4 reflected this position.[103] In addition, as noted earlier, this issue, together with the requirements regarding the involvement of a judicial/ administrative authority for approval of a plan which includes cross-class cram-down under article 11 (mentioned at 5.6 below) will be returned to in the second JCOERE Report.

5.5 Council of the European Union

Throughout 2017 and 2018, the Council considered the proposed directive. In a note from the Presidency to Coreper and the Council in May 2017, it was stated that the objectives of the proposal had received broad support from ministers at an informal meeting of the Justice and Home Affairs Council.[104] In the same note however, the President of the Council emphasized the need for flexibility in the implementation of the provisions within individual Member States. The Working Group tasked with reviewing the Proposal highlighted two areas which required greater scrutiny: the role of the national courts in insolvency matters and debtor in possession.[105]

Regarding the role of the courts, the Council was quick to point out that judicial or administrative authority involvement did not always equate to a less efficient procedure; instead it was the position of many delegations that the role of the judiciary in such matters was to act as an impartial safeguard.[106] As a result, the Council suggested that the proposal should be written in such a way as to allow Member States that desired decreased formality to do so, without making decreased formality a requirement for all Member States. At this point, it now appeared that committees within the Parliament – Legal Affairs and ECON – and the Council were opposed to mandatory decreased court formality. It is therefore unsurprising that the final wording reflected this position. Arguably, however, if Member States wished to decrease court involvement in insolvency matters, they could do so without the need for "encouragement" from a directive. As such, it is questionable whether the overall goals of the Proposal

[99] ECON Committee Opinion 33:

> "Paragraph 2 shall not apply to micro and small enterprise claims and workers' outstanding claims except if and to the extent that Member States ensure by other means that the payment of such claims is guaranteed at a level of protection at least equivalent to that provided for under the relevant national law transposing Directive 2008/94/EC."

[100] ECON Committee Opinion 33-34.

[101] Resultingly, the amended art 6(9) would have read:

> "Member States shall ensure that, where an individual creditor or a single class of creditors is or would be unfairly prejudiced by a stay … or a vulnerable creditor would encounter financial difficulties, the judicial or administrative authority may decide not [to] grant … or may lift a stay already granted in respect of that creditor or class of creditors, at the request of the creditors concerned. An unfair prejudice shall be deemed to exist at least where a creditor or class of creditors is facing considerable economic difficulties."

[102] As none of the amendments proposed to art 7 were accepted in the final draft, they have been discussed in Annex 1.

[103] See discussion on the Report by the Committee of Legal Affairs.

[104] Council of the European Union, Policy Debate of 19 May 2017 on the Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU File 2016/0359 (COD) 2 ("Policy Debate 19 May 2017").

[105] *idem* 2-5; It is worth noting that the Working Group had only considered arts 1 – 9 at this point in time.

[106] *idem* 3.

have now been nullified. It is interesting to note that the discussion around court involvement was not set in the broader context of the obligations to co-operate included in the EIR Recast.

In the period between May and November 2017, the Working Group identified three more areas in need of further consideration by Council, namely viability of the debtor, cross-class cram-down and second chance for honest entrepreneurs.[107] In relation to cross-class cram-down, it was noted that a majority of Member States considered there to be a need for provisions which allow the confirmation of a restructuring plan by a judicial or administrative authority in the event of the plan not being supported by a majority in one or more classes of creditors. With that said however, there were Member States which were hesitant to create such provisions; as such, further discussion on the area was considered beneficial.

In May 2018, the Council adopted a partial position (general approach)[108] on the proposed directive, however the position only pertained to Titles III, IV and V, thereby excluding the stay, cross-class cram-down, protection of new financing and decreased court formality. [109] The major development in the consultation process took place in October 2018, when the Council reached a full general approach on the proposed directive. The President, in an 87-page letter to the Council and Permanent Representatives Committee, highlighted a number of specific elements of compromise, including the stay and cross-class cram-down.[110] It was noted, however that there were still Member States in disagreement with the proffered compromises though a majority had accepted them.[111]

5.5.1 The Stay

There was considerable difference of opinion within Member States regarding the stay, some having a preference for short stays in the interest of creditors and others favouring a longer or indefinite stay in order to maximise the possibility of a successful restructure.[112] Even with the agreement on the stay, however, there was a clear, and in many cases, successful attempt by the Council to inject more latitude for the individual approaches of Member States into the PRD. Article 6(1) was amended to include an express provision allowing Member States the option to legislate for the refusal of a stay by a judicial or administrative authority in certain circumstances.[113] It could be argued, however, that this provision merely makes explicit what was already implicit in the wording of the first paragraph.[114] The Council also inserted 2b – now article 4 – into the Directive, which reads:

> "Member States may exclude certain claims or categories of claims from the scope of the stay of individual enforcement actions, in well-defined circumstances, where such an exclusion is duly justified and where:
>
> (a) where enforcement is not likely to jeopardise the restructuring of the business; or
>
> (b) where the stay would create unfair prejudice to the creditors of those claims."

The Council also proposed amending the conditions under which the stay can be lifted – now article 6(9) – to include where one or more creditors or classes of creditors would be unfairly prejudiced by the stay, where provided for by national law. The Council inserted another paragraph into article 6(9), which read:

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[107] Council of the European Union, Policy Debate of 30 November 2017 on the Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU File 2016/0359 (COD) ("Policy Debate 30 November 2017").

[108] Council of the European Union, Partial General Approach of 16 May 2018 of the Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU File 2016/0359 (COD).

[109] Neither the partial general approach not the general approach really addressed employee interests / employees as a class of creditors.

[110] Council of the European Union, General Approach of 24 September 2018 of the Proposal for a Directive of the European Parliament and of the Council on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures and amending Directive 2012/30/EU File 2016/0359 (COD) 3-6.

[111] *idem* 6.

[112] *idem* 4.

[113] "Member States may provide that judicial or administrative authorities can refuse to grant a stay of individual enforcement actions where such a stay is not necessary or where it would not fulfil the objective set out in the first subparagraph."

[114] The first paragraph of art 6(1) specifically refers to "a stay of individual enforcement actions *to support the negotiations of a restructuring plan*"[emphasis added] It would seem implicit therefore, that were the stay not to achieve this aim, that it could be rejected.

"Member States may limit the power, under the first subparagraph, to lift the stay of individual enforcement actions to situations where creditors had not had the opportunity to be heard before the stay came into force or before an extension of the period was granted by a judicial or administrative authority."[115]

Finally, as there are circumstances where national law requires a debtor to submit the restructuring plan to a judicial or administrative authority within 8 months, the Council attempted to insert article 6(7a) into the final text of the directive, however the Parliament declined to do so:

"By way of derogation from paragraph 7, where, according to national law, the restructuring plan is to be submitted within eight months from the start of the initial stay … to a judicial or administrative authority for confirmation, Member States may provide that that stay is extended until the plan is confirmed."

Although there were changes made by the Council to most of the subsections of article 7, these were largely of a minor nature. The substantial change made by the Council to article 7 was the insertion of article 6(6):

"Member States may provide that a stay of individual enforcement actions does not apply to netting arrangements, including close-out netting arrangements, on financial markets, energy markets and commodity markets, even in circumstances where Article 31(1) does not apply, if such arrangements are enforceable under national insolvency law. The stay shall, however, apply to the enforcement by a creditor of a claim against a debtor arising as a result of the operation of a netting arrangement.

The first subparagraph shall not apply to contracts for the supply of goods, services or energy necessary for the operation of the debtor's business, unless such contracts take the form of a position traded on an exchange or other market, such that it can be substituted at any time at current market value."

5.5.2 Protection of New Finance

With respect to the protection of new finance, the Council proposed some changes to (the then) article 16.[116] It sought to give individual Member States more control through the newly created article 17(2) and (3), which state respectively:

"Member States may provide that paragraph 1 shall only apply to new financing if the restructuring plan has been confirmed by a judicial or administrative authority, and to interim financing which has been subject to ex ante control.

Member States may exclude from the application of paragraph 1 interim financing which is granted after the debtor has become unable to pay its debts as they fall due."

It also rewrote the article 16(2)[117] which arguably has the effect of increasing the protection for new financiers:

"Member States may afford grantors of new or interim financing the right to receive payment with priority in the context of subsequent liquidation procedures in relation to other creditors that would otherwise have superior or equal claims to money or assets. In such cases, Member States shall rank new financing and interim financing at least senior to the claims of ordinary unsecured creditors."

This was rewritten as follows:

"Member States may provide that grantors of new or interim financing are entitled to receive payment with priority in the context of subsequent insolvency procedures in relation to other creditors that would otherwise have superior or equal claims"

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[115] The Council also attempted to grant Member States the ability to provide for a minimum period during which the stay could not be lifted, however this was not included in the final text.
[116] This was art 16 in the Commission draft and in the submission from the Council, however, the compromise text was renumbered as 17.
[117] Now art 17(4).

Arguably, the removal of the obligation on Member States ranking new financiers as "at least senior" to ordinary unsecured creditors leaves it at the protection of the new finance at discretion of the Member State, as the only obligation is that new financing and interim financing "are adequately protected". As noted above, article 17(4) merely states that Member States *may* provide that new financiers have priority in subsequent insolvency proceedings, not that they must. As such, it will be interesting to see if certain Member States only implement the basic requirement, for example, that generally, new financing cannot be declared void or unenforceable and that new financiers be exempt from liability but then make no changes to the priority of claims coming from new financiers in subsequent insolvency proceedings.

5.5.3 Cross-Class Cram-Down

The Council sought extensive changes to article 11. Some of these could be described as linguistic changes such as amending article 11(1)(a) to replace "fulfils the conditions in article 10(2)" with "complies with article 10(2)" and replacing the word "vary" with "increase" in article 11(2). However, the majority of changes were quite significant and offer considerable leeway to member states, in particular for those member states such as Ireland, which had operated a robust cross-class cram-down provision in the past. [118] To article 11(1) alone, the Council proposed nine different changes, one of which was outlined above. For clarity, the entirety of the Council's amended article 11(1) is below to enable proper comparison with the final text:[119]

> (1) Member States shall ensure that a restructuring plan which is not approved by **all voting classes** of affected parties **as provided for in Article 9(4)**, may be confirmed by a judicial or administrative authority upon the proposal of a debtor or (…) with the debtor's agreement, and become binding upon (…) dissenting **voting** classes where the restructuring plan **fulfils at least the following conditions**:
>
> (a) **it complies with** Article 10(2);
>
> (b) **it** has been approved by **the required voting classes of affected parties in accordance with paragraph 2;**
>
> **(c) it complies with the fairness test in accordance with paragraph 2a;**
>
> **(d) no class of affected parties can, under the restructuring plan, receive or keep more than the full amount of its claims or interests;**
>
> **By derogation from the first subparagraph, Member States may limit the requirement for the debtor's agreement to cases where debtors are SMEs."**

The final wording of the first paragraph is not exactly what the Council proposed, but it is more similar to its amendment than the original proposal; instead of "approved by all voting classes of affected parties as provided for in Article 9(4)…" it reads "approved by affected parties, as provided for in Article 9(6), in every voting class". The insertion of the word "voting" in relation to "dissenting voting classes" and the insertion of "fulfils at least the following conditions" remain in the final text.[120]

The wording of article 11(1)(b) provides for a declining set of requirements providing that a plan can be confirmed by a court where the plan:

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[118] General Approach; Note from the Presidency to Permanent Representatives Committee and the Council dated 24/09/2018 File 2016/0359 (COD) p.65-6.

[119] The wording of the Commission proposal was as follows; "Member States shall ensure that a restructuring plan which is not approved by each and every class of affected parties may be confirmed by a judicial or administrative authority upon the proposal of a debtor or of a creditor with the debtor's agreement and become binding upon one or more dissenting classes where the restructuring plan: (a) fulfils the conditions in art 10(2); (b) has been approved by at least one class of affected creditors other than an equity-holder class and any other class which, upon a valuation of the enterprise, would not receive any payment or other consideration if the normal ranking of liquidation priorities were applied; (c) complies with the absolute priority rule."

[120] Paragraph 1 of the final text reads; "Member States shall ensure that a restructuring plan which is not approved by affected parties, as provided for in art 9(6), in every voting class, may be confirmed by a judicial or administrative authority upon the proposal of a debtor or with the debtor's agreement, and become binding upon dissenting voting classes where the restructuring plan fulfils at least the following conditions…".

"has been approved by:

a. a majority of the voting classes of affected parties, provided that at least one of those classes is a secured creditors class or is senior to the ordinary unsecured creditors class; *or, failing that,*

b. at least one of the voting classes of affected parties or where so provided under national law, impaired parties, other than an equity-holders class or any other class which, upon a valuation of the debtor as a going-concern, would not receive any payment or keep any interest, or, where so provided under national law, which could be reasonably presumed not to receive any payment or keep any interest, if the normal ranking of liquidation priorities were applied under national law;"[121]

This final text is almost identical to the amendments proposed by the Council if one reads article 11(1)(b) in conjunction with paragraph 2, as the Council instructed in its amendment. The only substantial difference is that in the final text, the order of the two conditions is reversed and the words "failing that" have been inserted after the first condition, thereby giving it priority that it did not have in the Council amendment.

The final wording of article 11(1)(c) adopted some but not all of the amendment proposed by the Council in that it provides for ensuring "that dissenting voting classes of affected creditors are treated at least as favourably as any other class of the same rank and more favourably than any junior class".[122] The remainder of the amendment to 11(1)(c) via the newly inserted 11(2a), specifically that Member States require "a dissenting voting class of affected creditors is satisfied in full by the same or equivalent means if a more junior class is to receive any payment or keep any interest under the restructuring plan" was reformulated as a derogation instead (article 11(2)).[123] The scheme proposed by the Council therefore allows Member States to allow for the confirmation of plans where very little by way of consent has been secured. There is in fact a cascading set of requirements, allowing Member States to proceed to a robust restructuring framework, but also allowing for a more conservative approach for some member states. The view of the JCOERE Project Team is that this may amount to a failure of the policy goals of harmonisation and minimising the opportunities for forum shopping. The final wording of article 11(1)(d) and the derogation for SMEs in the PRD is the same as the amendments proposed by the Council.

The final paragraph of amendment 11(2a), namely that Member States may derogate from the earlier paragraph where it is necessary to achieve the aims of the restructuring plan as long as it is not unfairly prejudicial to affected parties, is now the second paragraph of article 11(2) in the Directive. The Council also tried to insert article 11(2b) which stated that "Article 10(3) shall apply *mutatis mutandis*", however this amendment was not included in the final text.

As has been demonstrated, the Council proposed quite considerable changes to the Commission text. In September 2018, the relevant bodies (the Parliament, the Council and the Commission) agreed to enter into interinstitutional negotiations, more commonly referred to as "a trilogue". The purpose of a trilogue is "to reach a provisional agreement on a text acceptable to both the Council and the Parliament";[124] as such, members of the three bodies took part in the negotiation. In March 2019, the Parliament voted to approve the compromise wording of the PRD. In a short debate, which took place the day before the vote, MEP Cofferati lamented the missed opportunity to ensure that the most vulnerable were properly protected, namely workers.[125] In his view, it would have been appropriate to extend the rights of workers to approve or reject restructuring plans concerning the organisational aspects of the company, such as plans involving layoffs and changes to working conditions. He also stated that employees should be treated preferentially compared to all other classes and opined that it should be mandatory for Member

[121] PRD, art 11(1)(b).
[122] PRD, art 11(1)(c). The Council amendment in its General Approach (n 110) mandated reading art 11(1)(c) in conjunction with art 11(2a).
[123] PRD, art 11(2): "By way of derogation from point (c) of paragraph 1, Member States may provide that the claims of affected creditors in a dissenting voting class are satisfied in full by the same or equivalent means where a more junior class is to receive any payment or keep any interest under the restructuring plan."
[124] 'Interinstitutional Negotiations for the Adoption of EU Legislation' (European Parliament Ordinary Legislative Procedure 2019) <http://www.europarl.europa.eu/ordinary-legislative-procedure/en/interinstitutional-negotiations.html> accessed 9th January 2020.
[125] Translated from European Parliament Debates 27 March 2019.

States to provide for a separate class for creditors. The Rapporteur responded that she was satisfied that the right approach was for employees to have the same protection as any other creditor. Strictly speaking, it is not correct to state that employees have the same protection as any other creditor, given that new financiers may receive preferential treatment. With that said, it may be a consequence of translating the response from German to English that this distinction was lost.

5.6 Conclusion

As of 20th June 2019, the final draft of the Directive was signed and was published in the Official Journal on 26th June with the implementation deadline set for 17th July 2021.[126] As has been demonstrated throughout this Chapter, many aspects of the Directive have seen substantial changes between its inception and its signing in 2019. Article 4(6) has transformed from being a clear requirement on Member States to decrease court formality to being a suggestion.[127] The primary amendment to article 6(1) was the inclusion of the second paragraph giving Member States the option to provide for judicial or administrative authorities refusal of a stay where it was viewed to be unnecessary where it would not support the negotiation of a restructuring plan.[128] Arguably, however, the insertion of this paragraph is of limited value; it is implied in the first paragraph of article 6(1) that the purpose of the stay is that it supports the negotiations of the restructuring plan, therefore is should only be granted in circumstances where it supports the negotiation process. Article 6(9)(a) was reformulated to make explicit that the stay can be lifted where it no longer fulfils the objective of supporting the negotiations on the restructuring plan and gave the original (a) as an example of such a case.[129] Article 6(9)(d), which states that if the stay gives rise to the insolvency of a creditor, it can be lifted where this is provided for under national law, was added. Again, the strength of this amendment is questionable; if it only applies in Member States where it is already a legal provision, then arguably, nothing is changing. Furthermore, it is possible that such provisions do more harm than good to the overall goal of harmonisation, It neither requires Member States who have these provisions to remove them, nor Member States who do not have them to introduce them.

The redrafting of article 11 is particularly significant regarding debates which had raged concerning the issue of priorities. The derogations provided allow for a broad range of practices and solutions to emerge once implementation has occurred.

As discussed previously, the primary changes to article 17 came from the Council, namely the insertion articles 17(2) and (3) and the rewriting of article 17(4); however, the wording of these articles means that their implementation can be classed as optional, rather than mandatory. Accordingly, one must once again question the degree to which the PRD achieves the central aim of harmonisation of the law across Member States if the protection for new finance may be significantly stronger in some jurisdictions than others.

5.7 Transition Chapter 6: Mapping the Preventive Restructuring Frameworks and the EU Directive: Part 1 – Introduction and Methodology

Chapter 6 will introduce the core research aspects of the JCOERE Project: The JCOERE Questionnaire. Split into 3 parts, Chapter 6 will focus on the first part, which discusses the current preventive restructuring frameworks in each of the contributing Member States. The Chapter begins by providing a benchmark to an already well-used and robust preventive restructuring procedure that has existed in Ireland since 1990. Chapter 6 will then provide a more detailed discussion of the research methodology employed in the JCOERE Project, as well as illuminating some of the challenges encountered by the team. It will also provide some general context for preventive restructuring as a background to the discussion of the responses from the first part of the questionnaire. Finally, the first part of the

[126] PRD, art 34.
[127] Article 4(6) states that Member States "*may*" put in place provisions limiting the involvement of a judicial or administrative authority in a preventive restructuring framework to where it is necessary and proportionate while ensuring that rights of any affected parties and relevant stakeholders are safeguarded."
[128] Article 6(1); "Member States may provide that judicial or administrative authorities can refuse to grant a stay of individual enforcement actions where such a stay is not necessary or where it would not achieve the objective set out in the first subparagraph."
[129] "[I]f it becomes apparent that a proportion of creditors which, under national law, could prevent the adoption of the restructuring plan do not support the continuation of the negotiations".

questionnaire responses will be described, essentially setting out what each contributing jurisdiction currently has in terms of preventive restructuring frameworks.