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   The Directive was approved by the European Parliament on 28 March 2019 and by the Council of Ministers on 6 June 2019. While both the Parliament and the Council had significant roles in shaping the final product, the Directive stems from a European Commission proposal on 22 November 2016. This proposal was in turn firmly anchored in the Capital Markets Union project. The Directive has three main elements: firstly, a ‘preventive’ restructuring framework; secondly, provisions on second chance/fresh start for ‘entrepreneurs’; and thirdly, more general provisions designed to enhance the efficiency of restructuring, insolvency and second chance procedures.

The overall objective is to reduce barriers to freedom of establishment and the free flow of capital stemming from differences in the laws and procedures of...
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EU Member States on restructuring and insolvency. The specific intention is that growth and jobs will flow. The Commission proposal suggested:

Boosting jobs and growth in Europe requires a stronger rescue culture which helps viable businesses to restructure and continue operating while channelling enterprises with no chance of survival towards swift liquidation, and gives honest entrepreneurs in distress a second chance. This proposal is an important step towards such a change of culture.2

1.03 The Directive concludes the Commission’s plan for legislative action in this area and it complements the recast Regulation on Insolvency Proceedings3 which came into force in June 2017. The Directive builds on earlier Commission initiatives in this area, most notably the 2014 Recommendation on a new approach to business failure and insolvency.4 According to the Commission, this Recommendation, lacking formal legal status, had only been partially implemented by Member States.5 The Directive differs in some important respects from the Recommendation, however, and adds significantly in various aspects. The Directive also differs significantly from the original Commission proposal, most notably by introducing the possibility of ‘relative priority’ between creditors rather than ‘absolute priority’ in the context of a restructuring plan and judicial/administrative approval of the plan.6

3 Regulation 2015/848 replacing Regulation 1346/2000. It should be noted that under Article 86 Member States are required to provide the Commission with a short description of their national legislation and procedures relating to insolvency and to keep this information regularly updated.
This book analyses the Directive in detail7 setting it in the context of broader international indicators and most notably Chapter 11 of the US Bankruptcy Code.8 The overall message in the book is that while more time could have been given to Member States to implement the 2014 Recommendation, the Restructuring Directive adds value and is likely to be particularly beneficial in those States that currently lack a developed restructuring framework for ailing businesses. A minimum measure of reform and harmonisation is practicable and achievable though the detailed measures contained in the Directive are open to comment and criticism in a number of respects.9 These points are elaborated upon at greater length throughout the book.

This introductory chapter consists of four substantive sections. The first section sets out the main features of the Directive. The second section looks at the background and considers the rationale of the Directive. The third section locates the Directive in the context of broader international developments including in particular Chapter 11 of the US Bankruptcy Code, the UNCITRAL Legislative Guide on Insolvency, and the World Bank Insolvency and Creditor Rights framework and its Doing Business project. Finally, the fourth section concludes.

1. MAIN FEATURES OF THE RESTRUCTURING DIRECTIVE

The European Commission have ‘sold’ the advantages of the Directive on various inter-related grounds. In short, debtors will have access to early warning tools that can enable them to detect a deteriorating business and lead to more restructurings at an early stage. This should facilitate the development of a new culture of preventive restructurings with viable enterprises in financial difficulties being able to access early restructuring procedures, wherever they are located in the EU. Under these procedures, the debtor will benefit from a

7 The Directive also contains other provisions particularly on debt discharge for individual debtors and more generally on improving the efficiency of insolvency, restructuring and debt discharge procedures, see Articles 20–24 and 24–28.


9 For some sharp criticism see H Eidenmüller, ‘The Rise and Fall of Regulatory Competition in Corporate Insolvency Law in the European Union’ (2019) 20 EBOR 547 who concludes at p 565 that the Restructuring Directive is an inefficient and harmful piece of legislation—it should be repealed’. See also by the same author ‘Contracting for a European Insolvency Regime’ (2017) 18 EBOR 273.
time-limited ‘breathing space’ from enforcement action in order to facilitate negotiations on a successful restructuring. Creditors benefit as well, as overall recovery rates should increase in a restructuring scenario. In order to enhance the possibility of a successful restructuring, there is provision for dissenting minority creditors and shareholders to be ‘trumped’ or outvoted under strict conditions and with due safeguards for their legitimate interests.

1.07 There is special protection for ‘new financing’ so as to further the prospects of a successful restructuring. While court involvement is seen as necessary to safeguard the interests of creditors and other shareholders, the intention is that flexible preventive restructuring frameworks will shorten court proceedings. Specialised courts, appropriately qualified insolvency or restructuring professionals and the use of technology should improve insolvency procedures in terms of efficiency and reduce their cost and length.

1.08 The benefits of the restructuring regime are also intended to apply to honest but insolvent individual entrepreneurs. Insolvent entrepreneurs are also allowed full discharge of their debt after a 3 year maximum period without further conditions though subject to anti-abuse safeguards. The benefits of the debt discharge regime may be extended by Member States to consumer debtors.

a. Access to the procedure

1.09 Where there is a likelihood of insolvency but not where the debtor has reached the stage of insolvency as understood under national law, Member States must provide debtors with access to a preventive restructuring framework or procedures. The framework is intended to enable them to restructure, with a view to preventing insolvency and ensuring their viability. A consequence of this is intended to be the protection of jobs and the continuation of business activity. Member States may introduce a viability test but this test is only intended to assess viability and the conduct of the test should not detrimentally affect the debtor’s assets. The restructuring framework may consist of a number of measures or provisions and it may be that Member States, after implementation of the Directive, are left with a number of partially overlapping regimes to deal with financially stretched debtors.

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10 Articles 1(1) and 1(2)(h).
11 Articles 19–23.
12 Article 1(4).
13 Article 4(1).
14 Article 4(3).
15 Article 4(5).

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Member States are also left with a number of implementation options in terms of the bodies or natural or legal persons to which the restructuring regime may be applied. The Directive does not apply to certain financial institutions as set out in Article 1(2) including credit institutions (banks), insurance undertakings, investment firms and collective investment undertakings. These exclusions mirror, if not exactly corresponding with, those contained in the recast Insolvency Regulation – Regulation 2015/848. It seems that the Restructuring Directive should not be applied to those entities largely because they are the subject of different, and possibly conflicting, legal regimes. Natural persons who are not entrepreneurs are also mentioned in Article 1(2) but Article 1(4) allows Member States to extend the debt discharge provisions, but not the restructuring framework as a whole, to insolvent natural persons who are not entrepreneurs. In other words, consumer debtors may be allowed the possibility of debt discharge.

One can easily imagine many Member States exercising the exclusion option, rather than the extension option. The vast majority of business in that particular country may be transacted in the corporate form. Moreover, certain professions in that country may have formal disciplinary and ethical requirements that sit rather uneasily with the norms postulated by the Restructuring Directive.

The general rule under the Directive is that the preventive restructuring framework is available only on application by the debtor. Member States, however, may also permit creditors’ and employees’ representatives to apply with the agreement of the debtor. Member States may also go in the opposite direction and limit the requirement to obtain the debtor’s agreement to cases where debtors are SMEs – micro, small and medium-sized enterprises. It is not spelled out in the Directive but, applying a standard principle of interpretation that the greater includes the smaller, if Member States can limit the requirement to all SMEs they could limit it only to some SMEs, for example medium-sized enterprises rather than small or micro enterprises.

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16 Under Article 1(3) Member States may also exclude other financial entities where national supervisory or regulatory authorities have similarly wide powers of intervention comparable to those applicable in the case of banks etc.
17 ‘Entrepreneurs’ are defined in Article 2(1)(8) as natural persons ‘exercising a trade, business, craft or profession’.
18 Article 4(1).
19 Article 4(8).
20 Ibid.
b. Debtor-in-possession

1.13 The Directive has a debtor-in-possession norm, that is, the general principle is that the debtor is to be left in control of its assets and the day-to-day operation of the business, though there are three qualifications to this norm. The first qualification is that a regime of only partial debtor control seems to be acceptable. So if a Member State required the automatic appointment of a restructuring professional in all cases to act alongside the debtor, this would seem to pass muster. Secondly, the appointment of a restructuring professional on a ‘case-by-case basis’ is expressly permitted though the factors that would warrant such an appointment are not articulated. Thirdly, there are certain circumstances where Member States shall require the mandatory appointment of the restructuring practitioner in every case. These are: (i) where a general stay of individual enforcement action is granted by the relevant authorities who consider such an appointment necessary to safeguard the interests of the parties; (ii) where cross-class cram-down is envisaged; or (iii) where the debtor or a majority of creditors requests the appointment.

1.14 Where a mandatory appointment is envisaged, the role of the restructuring practitioner seems to be limited to that of assisting the debtor and creditors in negotiating and drafting the restructuring plan. This role is more limited than that in the general definition of restructuring practitioner who according to Article 2(1)(12) may be (i) somebody assisting the debtor in drafting or negotiating a restructuring plan; (ii) supervising the debtor during the period and reporting to the relevant authorities; and (iii) assuming partial control of the debtor’s affairs. Therefore, there is not one conception of the restructuring practitioner who may be variously a manager, monitor or supervisor.

1.15 The relevant provisions do not pass direct judgement on whether the appointment of a restructuring practitioner may take the form of more or less strict ‘management displacement’, with the existing board of directors losing their management responsibilities in respect of the debtor’s affairs to an outside appointee. The directors remain in office but the new appointee takes over the role of directing the debtor’s affairs and planning the restructuring. The existing directors only have a role in relation to management and planning if they are called upon by the restructuring practitioner, and to the extent that

21 Article 5.
22 For criticism see H Eidenmüller, ‘The Rise and Fall of Regulatory Competition in Corporate Insolvency Law in the European Union’ (2019) 20 European Business Organization Law Review 547 at pp 559–60: ‘This requirement restricts contractual freedom, reduces flexibility and makes the restructuring process more complicated and costly. Engaging advisors or experts should have been left to the participating stakeholders ….'
they are called upon. The implication from Article 5(1), however, is that such an arrangement would be impermissible. Article 5 clearly states that debtors remain at least partially in control of their assets and day-to-day operations of their business.

c. Moratorium/stay on individual enforcement actions

There is provision in Article 6 for a stay of individual enforcement actions. The stay is intended to give debtors a respite on claims from creditors and to facilitate negotiations on a restructuring plan.23 There may be little prospect of debtor rehabilitation if creditors deprive the debtor of assets that may be essential to the carrying on of the debtor’s new or rehabilitated business. From the wording of Article 6, it appears that the stay is not intended to be automatic; in other words, kicking in as a matter of course once restructuring proceedings are opened or there is an application to open restructuring proceedings. It is not like the automatic stay that applies once there is a filing under the US Bankruptcy Code and in particular under the reorganisation Chapter 11. It seems, however, that there is nothing to stop Member States from instituting a mandatory automatic stay and thereby meeting their obligations under Article 6 provided that there are appropriate provisions that allow the stay to be lifted in certain circumstances.

What Article 6 envisages principally, however, is a more tailored, discretionary stay that arises on application to the court but one which could, nevertheless, cover all claims including secured claims and preferential creditors24 though with an exception for employee claims unless payment of these is guaranteed for the duration of the preventive proceeding.25 The initial period of the stay is confined to 4 months26 though Member States may permit its extension for a total maximum period of no more than 12 months.27

There are certain requirements that should be fulfilled before the stay can be extended, for example where relevant progress has been made in negotiating the restructuring plan and continuation of the stay does not unfairly prejudice the rights or interests of any affected parties.28 Alternatively, the stay may be limited to one or more creditors or categories of creditors29 or lifted altogether.

23 Article 6(1).
24 Article 6(2).
25 Article 6(4).
26 Article 6(6).
27 Article 6(8).
28 Article 6(7).
29 Article 6(3).
such as where the stay no longer supports negotiations on a restructuring plan because the plan does not have the necessary measure of creditor support, or where the stay has caused insolvency on the part of a creditor. Member States, for instance, may provide that the stay does not apply to netting arrangements, including close-out netting arrangements on financial markets, energy markets and commodity markets.

1.19 Under Article 7, the commencement of the stay suspends the opening of insolvency proceedings and any obligation on the part of directors to file for the opening of insolvency proceedings. Any mandatory insolvency filing rules for directors will be suspended during the period of the stay. Creditor will also be suspended from initiating insolvency proceedings. Member States may, however, specify that such suspension will not operate where the debtor is cash flow insolvent, that is, unable to pay its debts as they fall due. The relevant authorities may, however, decide to keep the stay in place if it is not in the general interest of creditors to open insolvency proceedings.

1.20 Creditors subject to the stay and with unpaid claims from the commencement of the preventive restructuring framework are precluded from withholding performance, or terminating or otherwise modifying essential executory contracts solely because the debts had not been paid. For these purposes, ‘essential executory contract’ is to be understood as an executory contract which is necessary for the continuation of the day-to-day operations of the business (including contracts concerning supplies, the suspension of which would lead to the debtor’s activities coming to a standstill). As part of the general philosophy of maximum flexibility underpinning the Directive, the executory contracts measure may be extended by Member States to non-essential executory contracts. It may also be cushioned by an obligation to provide creditors at risk of unfair prejudice from the measure with appropriate safeguards.

1.21 The debtor will also benefit from a more general protection against ipso facto clauses – so that suppliers with contractual rights to terminate the supply contract solely based on the insolvency will not be able to invoke such rights.

30 Article 6(9).
31 Article 7(6).
32 Article 7(4) first para.
33 Article 7(4) third subpara.
34 Article 7(5).
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d. The restructuring plan and confirming the plan

The debtor has the right to submit a restructuring plan and Member States may decide whether, and when, creditors and restructuring professionals also have the right to submit a plan. Only ‘affected parties’ have a right to vote on the plan, and as a corollary, unaffected parties have no right to vote on the plan. Member States may decide to exclude certain persons from having a right to vote, specifically: (i) shareholders; (ii) creditors whose claims rank below the claims of unsecured creditors in accordance with liquidation priorities; and (iii) parties related to the debtor with a conflict of interest under national law.

Affected parties are divided into classes with a view to adopting the plan and these classes should reflect a sufficient commonality of interest. Secured creditors should be in a separate class from unsecured creditors as a minimum. Member States may also specify that workers’ claims are a class of their own. Some leeway is given to SMEs for Member States may enable them to place all creditors in the same class. The Directive is not totally clear on whether this freedom given to SMEs also applies in respect of secured creditors; in other words whether SMEs may put secured and unsecured creditors in the same class. Because of the general respect accorded property rights, the better view is that secured and unsecured creditors should not be put in the same class except for the unsecured portion of a secured claim.

The court will examine class formation issues either when the plan is submitted for confirmation or, if Member States provide, at an earlier stage. The rules laid down in the Directive on approval of a restructuring plan are quite elaborate. The relevant classes consist of affected parties and a majority in amount of their claims or interests must be obtained in a particular class before that class is deemed to have approved the plan. It is a majority in value rather than a majority in number though Member States are free to lay down an additional ‘majority in number’ requirement. The threshold for acceptance is set by each Member State. It could be as low as a simple majority in

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35 Article 9(1).
36 Article 9(2): ‘Parties that are not affected by a restructuring plan shall not have voting rights in the adoption of that plan.’
37 Article 9(3).
38 Article 9(4).
39 See also recitals 42 and 44 of the preamble to the Regulation and the statement in recital 44: ‘It should be possible for Member States to provide that secured claims can be divided into secured and unsecured parts based on collateral valuation.’
40 Article 9(5).
41 Article 9(6).
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value but must not be higher than 75 per cent in the amount of claims or number in each class. Member States may also set a participation threshold for each vote. Therefore, the percentage in value requirement that has to be fulfilled may depend on the percentage of creditors that actually participate in the voting and the proportionate value of their claims.

1.25 Confirmation of the plan by a court or administrative authority is also required in certain circumstances such as where the plan either (i) affects the claims or interests of dissenting affected parties; (ii) provides for new financing; or (iii) involves a loss of more than 25 per cent of the workforce.\(^\text{42}\) There are also certain conditions that have to be met before the court/administrative authority can confirm the plan. These include, where there are dissenting creditors, whether the plan complies with the ‘best interest of creditors’ test.\(^\text{43}\) This test applies even if the class as a whole is prepared to accept the plan. This means that no dissenting creditor is worse off under the plan than they would be if the normal ranking of liquidation priorities were applied either in a (i) liquidation; (ii) going-concern sale; or (iii) in the next-best-alternative scenario if the plan was not confirmed.

1.26 Dissenting creditors are well looked after though it may be difficult to calculate in practice what these dissentients would receive if the plan was not approved but rather some alternative scenario was implemented. The relevant judicial/administrative authorities are also to refuse confirmation of the plan if it does not pass a ‘feasibility test’, that is, if it does not have a reasonable prospect of preventing insolvency or ensuring the viability of the debtor’s business.\(^\text{44}\)

1.27 If all the relevant classes have not approved the plan, there is still room for judicial/administrative confirmation or ‘cross-class creditor cram-down’ as it is called. In these circumstances, the plan must meet the ‘best interests of creditors’ and ‘feasibility’ tests. In addition, it must have been approved by a majority of classes of affected parties. But at least one of those classes must be either (i) a secured creditor class; or (ii) senior to the ordinary unsecured creditor class; or (iii) a class of affected or impaired parties other than a class of shareholders or a class that would not receive anything on a going-concern value of the debtor’s business.\(^\text{45}\) There is a somewhat circular definition of ‘affected parties’ in Article 2(2) as a class whose claims or interests are ‘directly affected by a restructuring plan’.

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\(^{42}\) Article 10(1).

\(^{43}\) See Articles 10(2)(d) and 2(6).

\(^{44}\) Article 10(3).

\(^{45}\) Article 11(1).
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There is no definition of ‘impaired parties’ as such though recital 54 of the preamble contains a statement that the ‘impairment of creditors’ should be understood to mean that there is a reduction in the value of their claims. This statement is vague since it could refer to either face value or real economic value. If repayment periods are stretched out, or interest rates are cut, then the real economic value is reduced even though the face value may remain the same. The implication in the Directive, however, is that being an ‘impaired party’ suggests a more radical curtailment of rights than merely an ‘affected party’. Member States may substitute ‘impaired party’ for ‘affected party’ and the context implies this is a more stringent requirement. Member States may also increase the number of classes which need to approve the plan but they cannot require the consent of all such classes. Moreover, no class may keep more than the full amount of its claims.46

One of the most controversial aspects of the Directive is that the prima facie rule is one of relative priority rather than absolute priority. Dissenting classes must be treated at least as favourably as any other class of the same rank and more favourably than any junior class. The basic rule under the US Bankruptcy Code is one of absolute priority rule, that is, a senior class of dissenting creditors should be paid in full before a junior class receives anything.47 It is not just giving them a little bit more than a class of senior creditors as a rule of relative priority implies; instead it is paying them in full before junior creditors have the chance to receive anything. The justifications for the US principle are that it reflects the normal scheme of liquidation priorities; provides greater certainty for debt investors; and enables capital to businesses to be allocated more efficiently. But the assumption under the US Bankruptcy Code is that businesses entering the process are unable to pay their debts whereas under the Restructuring Directive the assumption is somewhat different. The Directive is designed for situations where, admittedly, there is a likelihood of insolvency, but the objective is to prevent insolvency and ensure the debtor’s viability. This may justify a different default rule but it should be noted that Member States may make provision for an absolute priority rule rather than relative priority when implementing the Directive. This means satisfaction in full of senior creditors before a more junior class can receive any payment or keep any interest under the plan. But there is also scope to temper the rigours of absolute priority to achieve the aims of the restructuring plan and where such deviation does not unfairly prejudice the rights or interests of any affected parties.48

46 See Article 11(1)(d): ‘no class of affected parties can, under the restructuring plan, receive or keep more than the full amount of its claims or interests’. See generally S Paterson, ‘Rethinking Corporate Bankruptcy Theory in the Twenty-First Century’ (2016) 36 Oxford Journal of Legal Studies 697.
47 Section 1129 US Bankruptcy Code.
48 Article 11(2).
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1.30 Member States may exclude shareholders from voting on the plan but in these circumstances they must ensure ‘by other means’ that shareholders cannot ‘unreasonably’ prevent the adoption of a plan or indeed its implementation.\footnote{Articles 12(1) and 12(2).} Member States can adapt what is considered ‘unreasonable’ to take into account whether the debtor is an SME or a large enterprise, what the proposed restructuring is, and the type of shareholder.\footnote{Article 12(3).} The position of employees was also hotly contested during the negotiations on the Directive. The Directive came down in favour of the view that Member States are to ensure that workers’ rights under individual and collective, national and EU law must not be affected, including the right to collective bargaining and to information and consultation.\footnote{Article 13.}

1.31 Plans that are confirmed by a court or administrative authority are binding upon all affected parties.\footnote{Article 15(1). It is also provided in Article 15(2) that creditors who are not involved in the adoption of a restructuring plan are not affected by the plan.} The Directive does not spell out the situation where there is no judicial or administrative confirmation as such but the necessary majority of affected parties in each class has instead been obtained. Recital 53 states, however, that such a plan should always be adopted. Valuation is an important issue in the context of the confirmation of a restructuring plan by a court or administrative authority. The relevant authority must assess whether the ‘best interest of creditors’ test has been met; and in cross-class cram-down, whether at least one affected or impaired class other than shareholders or those who would receive nothing in a going-concern valuation has approved the plan.\footnote{Article 14.} Properly qualified experts may be appointed to assist the relevant authority on valuation matters.\footnote{Article 14(2).} There is also provision for a dissenting affected creditor to lodge a challenge on valuation matters.\footnote{Article 14(3).}

1.32 Article 16 makes provision for appeals more generally. A decision to confirm or reject a restructuring plan may be appealed. Appeals from a judicial authority go to a higher judicial authority and from an administrative authority to a judicial authority. On appeal, a court may set aside the plan or confirm it with or without amendments. A pending appeal is not supposed to have suspensive force but Member States may derogate from this principle and suspend the execution of the plan if this is necessary and appropriate to safeguard the interests of a party.

\footnote{Article 12(1) and 12(2).}
\footnote{Article 12(3).}
\footnote{Article 13.}
\footnote{Article 15(1). It is also provided in Article 15(2) that creditors who are not involved in the adoption of a restructuring plan are not affected by the plan.}
\footnote{Article 14.}
\footnote{Article 14(2).}
\footnote{Article 14(3).}
e. New financing and restructuring related transactions

Member States shall ensure that new and interim financing is not declared void and that the grantors of such finance do not incur civil, administrative or criminal liability merely because the financing is detrimental to the general body of creditors.\(^{56}\) Other grounds for invalidation may, however, be present and the protection can also be restricted to restructuring plans that have been confirmed by the court. Compared with the equivalent provision in the US Bankruptcy Code – s 364 – the Directive is relatively sparse in terms of details on new or interim financing. New financing is, however, defined in Article 2(7) as new financial assistance provided to implement a restructuring plan and that is included in the plan. Interim financing is defined as new financial assistance provided during the stay of individual enforcement actions that is reasonable and immediately necessary for the debtor’s business to continue operating, or to preserve or enhance the value of that business.\(^{57}\)

The sparseness comes particularly with the extent of the protection and priority given to grantors of new or interim financing. Member States may stipulate that such grantors have priority in a subsequent insolvency over other creditors who would otherwise have superior or equal claims. There is nothing, however, on the conditions that might have to be satisfied before gaining such priority.\(^{58}\)

Nevertheless, the Directive does fill in some blanks on wider restructuring related transactions. Where a debtor subsequently becomes insolvent, certain transactions that are reasonable and immediately necessary for the negotiation of a plan cannot be declared void or unenforceable merely because they are detrimental to the general body of creditors unless there are some other additional grounds laid down by national law.\(^{59}\) The transactions that the Directive has in mind include as a minimum the payment of fees and negotiating costs for the plan, professional advice in close connection with the restructuring as well as the wages of employees.

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56 Article 17.
57 Article 2(8).
58 Article 17(4).
59 Article 18.
1.36 Member States are obliged to ensure that, where there is a likelihood of insolvency, directors as a minimum have regard to the interests of creditors, shareholders and other stakeholders; the need to take steps to avoid insolvency; and the need to avoid deliberately negligent conduct that threatens the viability of the business.60

1.37 Member States are required to have competent and well-trained courts and administrative authorities as well as restructuring and insolvency practitioners and to put in place appropriate oversight and regulatory mechanisms to supervise the relevant practitioners. It should be noted that in this context the Directive ranges far beyond restructuring and also encompasses insolvency and second chance procedures more generally. But the language is aspirational rather than directional. For instance, there is a statement that procedures should be handled in an efficient manner and with a view to expeditious treatment of matters.61 The same aspirational language appears in relation to insolvency and restructuring practitioners including on the development and adherence to codes of conduct; rules on remuneration that are consistent with the objective of achieving efficiency; and appropriate settlement of disputes.62

1.38 There is more direction when it comes to the provisions on data collection. Both the recast Insolvency Regulation and the Restructuring Directive contain provisions that aim to enhance the quality of the information available to stakeholders and the European Commission on the restructuring and insolvency procedures open in Member States.63

2. BACKGROUND – RATIONALE OF THE DIRECTIVE?

1.39 The reasons behind the Restructuring Directive appear to be quite simple – growth and jobs.64 The 2008 global financial crisis produced asymmetric shocks across Europe. Since then the economic recovery has been sluggish and

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60 Article 19.
61 Article 25(b).
62 See Article 26 and also Article 27 on the supervision and remuneration of practitioners.
63 See Article 29 of the Restructuring Directive and Articles 24–27 of the recast Insolvency Regulation (Regulation 2015/848) on the establishment and interconnection of national insolvency registers and Article 86 on the provision of information relating to national insolvency law.
there is persistently high unemployment particularly in some Member States. There is the need for an EU-wide response and the Restructuring Directive is part of that response. The Directive builds on the Recommendation on a new approach to business failure and insolvency. It is part of the Juncker Plan and the Capital Markets Union project and has been spoken of as Europe’s response to Chapter 11 of the US Bankruptcy Code. The objective of Chapter 11 is said to be ‘to provide a debtor with the legal protection necessary to give it the opportunity to reorganize, and thereby to provide creditors with going-concern value rather than the possibility of a more meagre satisfaction of outstanding debts through liquidation’. Professors Warren and Westbrook suggest that Chapter 11 deserves a prominent place in ‘the pantheon of extraordinary laws that have shaped the American economy and society and then echoed throughout the world’. Chapter 11 has been cited as a great success by its proponents and certainly as a model for European restructuring laws. In this section, we will trace the origins of the Directive through: (i) the Recommendation on a new approach to business failure and insolvency; (ii) the Capital Markets Union project; and (iii) the original European Commission proposal for the Restructuring Directive.

a. Recommendation on a new approach to business failure and insolvency

The European Commission recommendation in 2014 on a new approach to business failure and insolvency was part of the Europe 2020

71 C (2014) 1500 final; and see also Commission Communication, A New European Approach to Business Failure and Insolvency, COM (2012) 742. The Recommendation also contains provisions on a fresh start for ‘honest’ entrepreneurs. In this book, the expressions ‘insolvency’ and ‘bankruptcy’ are generally used...
strategy designed to foster economic recovery and sustainable growth. The objective was to create a situation where economic and social systems are adaptable, resilient and fair and where human values are respected. The Recommendation encouraged Member States to ‘put in place a framework that enables the efficient restructuring of viable enterprises in financial difficulty’ and to provide for ‘minimum standards on … preventive restructuring frameworks’.

The evaluation carried out by the Commission on implementation of the Recommendation singled out six features for particular attention. It suggested that these six elements increase the efficiency of restructuring procedures and each of them should be present in national law. All of them are now present in the Restructuring Directive. The six elements are:

1. The possibility to file early with the objective of avoiding insolvency
2. The position of the debtor, that is, debtor-in-possession
3. The possibility of a stay on individual enforcement actions
4. Adoption of the restructuring plans by creditors
5. The protection for new finance granted in restructuring procedures
6. The involvement of courts when third party rights could be affected

But why make these features compulsory and turn the Recommendation into something harder and possibly less flexible? After all, it appears that modern restructuring procedures already exist in most, if not all, Member States.
seems that European insolvency law has gone through a remarkable transformation over the past decade or so with France being a good example of a jurisdiction that has carried out major reforms through the introduction of Sauvegarde (Safeguard), Accelerated Financial Sauvegarde and Accelerated Sauvegarde restructuring procedures.  

The justification for Commission action appears to be the incomplete and inconsistent implementation of the Recommendation. The Commission evaluation concludes that while ‘the Recommendation has provided useful focus for those Member States undertaking reforms in the area of insolvency, it has not succeeded in having the desired impact in facilitating the rescue of businesses in financial difficulty’. It has been suggested that in some countries restructuring procedures are completely absent, and in other cases, the procedures may be cumbersome and inefficient and have the effect of transferring wealth to ‘out of the money’ managers, shareholders and creditors. Other inefficiencies include prolonging the life of financially unviable enterprises. These may have detrimental consequences for healthy competitors and the overall soundness of the economy since it impedes accomplishing the objective of putting assets to their most effective use.

Nevertheless, Member States were given very little time to implement some of the suggestions made in the 2014 Recommendation which, after all, was not legally binding. There is a suspicion that the political imperatives of the Capital Markets Union project pushed the Commission into legislative mode quite quickly. It is certainly the case that legislative action at national level did not stand still in 2014 or in 2016.
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1.45 In the intervening years, various EU Member States have also adopted legislation to promote restructuring. For instance, a 2015 Polish Restructuring Law develops a variety of restructuring procedures that are intended to give economically viable but financially distressed businesses a ‘fresh chance’ as well as speeding up and enhancing the effectiveness of restructuring and bankruptcy proceedings.\(^83\) Croatia in 2017 introduced a new Law on the Procedure for Extraordinary Administration of Companies of Systemic Importance for Croatia (the EA) Act and this new law was then used for the successful restructuring of the *Agrokor* group in 2018.\(^84\) In 2017 Italy introduced the ‘Alert and Assisted’ arrangement procedures. Portugal legislated for a new law on out-of-court corporate restructuring in 2018 and also made provision for a new player on the insolvency scene – the corporate restructuring mediator.\(^85\)

1.46 These reforms learn from those that have already been in place in other EU States\(^86\) such as, for instance, France, which was a trend setter with the introduction in 2006 of Safeguard (fr. Sauvegarde), and later Accelerated Financial Safeguard and Accelerated Safeguard procedures.\(^87\) The 2018 World Bank *Doing Business* report singles out France\(^88\) for having over a period of time ‘implemented insolvency reforms that brought them closer to internationally recognized good practices—particularly through the introduction and improvement of restructuring procedures’.

1.47 Cyprus is an example of a country that has borrowed directly from the experience in another EU State. It reformed its laws in 2015 with the introduction of a new examinership procedure that was closely modelled on an Irish example dating back to 1990.\(^89\) In Ireland, the examinership procedure is a court-supervised process available to viable but financially distressed companies. The restructuring plan is agreed upon outside of court, but the court must confirm it. Before granting approval, the court will need to be satisfied that the plan is not unfairly prejudicial to any class of creditors or is simply a

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plan which purports to avoid tax. The ‘unfairly prejudicial’ test effectively requires an assessment that creditors are treated no worse under the plan than they would be in a likely alternative scenario such as the liquidation of the company’s assets. In Cyprus, the procedure has been little used. It seems that court procedures in Cyprus are seen by many users as slow and unwieldy and this discourages likely candidates for business restructuring from making full use of the new procedure.

b. **Action plan on building a Capital Markets Union**

The Action Plan on Building a Capital Markets Union\(^90\) is designed to strengthen Europe’s economy and stimulate investment with a view to creating employment. The Action Plan stresses the fundamental importance of stronger capital markets in providing new sources of funding for business, helping to increase options for savers and making the economy more resilient. The free flow of capital is one of the core foundation stones on which the EU is built but, as the Action Plan points out, Europe’s capital markets are still relatively underdeveloped and fragmented despite the progress over the past 50 years. While the EU economy is as big as that of the US, the EU’s equity markets are less than half the size of those in the US and its debt markets less than a third of the size. Moreover, there are even bigger gaps between individual EU Member States. The Action Plan suggests that more integrated capital markets will lead to efficiency gain inter alia by unlocking more investment from the EU and the rest of the world: better connecting financing to investment projects and increasing competition.\(^91\)

The Action Plan was accompanied by a staff working document\(^92\) that detailed various perceived obstacles in the growth path. It highlighted persistent barriers to the cost effective reorganisation of viable companies in the EU, and inefficient and divergent insolvency proceedings. These prevented speedy debt restructuring since non-performing loans were more difficult to resolve without effective restructuring and insolvency tools. There were also difficulties for investors in assessing credit risk, particularly in respect of cross-border investments given that there were divergent insolvency regimes in the EU. Moreover, there were incentives for ailing companies which do not have effective early restructuring possibilities in their home country to relocate to

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\(^91\) See generally the Action Plan at pp 3–4.

Member States with more effective systems. Minority creditors might be adversely affected by the application of a different insolvency regime even though the new regime could be beneficial to the general body of creditors and the debtor company as a whole. In addition, the high costs of relocation made it very difficult, if not impossible, for smaller enterprises (SMEs) to benefit from better restructuring possibilities in other Member States. On the other hand, the convergence of insolvency and restructuring regimes facilitated greater legal certainty for cross-border investors. It also encouraged the timely restructuring of viable companies in financial distress.

c. The Restructuring Directive proposal

The objectives of insolvency law have often been spoken of as being to restructure and rescue viable businesses and to liquidate non-viable ones as efficiently as possible. When the Restructuring Directive proposal was launched, the explanatory memorandum firmly located the Directive in the context of the jobs and growth agenda driving EU policymakers. The explanatory memorandum references these propositions though not in so many words and puts more of an emphasis on the rescue objective. It also asserts that a higher degree of harmonisation in insolvency law is essential for a well-functioning single market and for a true Capital Markets Union. It would ensure greater legal certainty for cross-border investors; reduce credit risk; deepen financial integration; lower costs of obtaining credit and increase EU competitiveness. This is certainly a tall order and it remains to be seen whether these generally laudable objectives will necessarily be accomplished in practice.

The memorandum goes further, however, and attempts to put some figures on the benefits that might be obtained from the Directive:

[I]n the EU, 200 000 firms go bankrupt each year (or 600 a day), resulting in 1.7 million direct job losses every year. One in four of these are cross-border insolvencies, i.e. they involve creditors and debtors in more than one EU Member State. A significant percentage of firms and related jobs could be saved if preventive procedures existed in all Member States where they have establishments, assets or creditors.


95 COM (2016) 723 final at p 1.

96 COM (2016) 723 final at pp 2–3.
3. CONFORMITY OF THE RESTRUCTURING DIRECTIVE WITH INTERNATIONAL DEVELOPMENTS

In general terms, the Restructuring Directive appears to be fully in line with international developments in the business restructuring sphere. These developments include the United Nations Commission on International Trade Law (UNCITRAL) Legislative Guide on Insolvency,97 the World Bank Principles for Effective Insolvency and Creditor/Debtor Regimes98 and the World Bank Doing Business project. These insolvency standards are intended as a tool or guide enabling States to improve their relevant laws but have also been used more explicitly as an evaluation tool that enables national laws to be judged and ranked.99

Many of these initiatives build upon Chapter 11 of the US Bankruptcy Code.100 As one US court put it, ‘the purpose of [Chapter 11] is to provide a debtor with the legal protection necessary to give it the opportunity to reorganize, and thereby to provide creditors with going-concern value rather than the possibility of a more meagre satisfaction of outstanding debts through liquidation’.101

a. UNCITRAL Legislative Guide on Insolvency

UNCITRAL is an offshoot from the United Nations (UN). It has produced the most comprehensive text – the 2014 Legislative Guide on Insolvency – setting international standards in respect of insolvency and restructuring and


99 The directive does not specifically deal with the situation where an ailing enterprise has assets in more than one State or the administration of its affairs in insolvency proceedings requires assistance from foreign countries – ‘cross-border insolvency’. In this area, UNCITRAL has been preeminent with its Model Law on Cross Border Insolvency – see http://www.uncitral.org/uncitral/en/uncitral_texts/insolvency/1997Model.html (accessed 26 January 2021). Legislation based on the Model Law has been adopted in 46 States in a total of 48 jurisdictions – see https://uncitral.un.org/en/texts/insolvency/modellaw/cross-border_insolvency/status (accessed 26 January 2021).


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stating clearly that such laws are critical in enabling a State to achieve the benefits of integration with the international financial system. In its view, such laws and institutions should ‘promote restructuring of viable business and efficient closure and transfer of assets of failed businesses, facilitate the provision of finance for start-up and reorganization of businesses and enable assessment of credit risk, both domestically and internationally’.102

1.55 The Legislative Guide employs a sophisticated and flexible repertoire of rules103 though it undoubtedly borrows heavily from the US Bankruptcy Code and in particular Chapter 11. The Guide, which now comes in four parts, is made up of over 200 recommendations in total divided into over 20 topics plus a detailed commentary.104 The commentary may stress the importance of a particular issue or principle and then justify a series of recommendations that give effect to that principle. It may contain a comparative analysis in situations where there is considerable cross-country variation on a particular topic, presenting and discussing alternative approaches and evaluating such approaches. The commentary also serves an important validation function by registering the fact that the views advanced by particular delegates have been listened to, even if they were not ultimately adopted, and also by setting out the reasons in favour of particular approaches.

1.56 The flexibility of the UNCITRAL Guide is demonstrated in relation to debtor-in-possession versus management displacement in the context of restructuring proceedings. The Guide states that different approaches may be taken on this issue including:105

1. retention of full control by the debtor, that is, debtor-in-possession with appropriate safeguards including varying levels of control of the debtor and debtor displacement in certain circumstances;
2. limited displacement where the debtor operates the business subject to the supervision of an insolvency representative with an appropriate division of responsibilities between the two;
3. total displacement of the debtor in favour of an insolvency representative.

102 See UNCITRAL Legislative Guide on Insolvency Law at p 10.
104 The original guide (Parts 1 and 2) was formulated in 2004, a third part on the treatment of enterprise groups in insolvency was added in 2010 and a fourth part on directors’ obligations in the period approaching insolvency was added in 2013.
105 See Recommendation 112.
Unlike the norm in the US Chapter 11, the UNCITRAL Guide does not recommend adoption of debtor-in-possession as the general norm in respect of corporate reorganisation. While Chapter 11 allows an outside bankruptcy trustee to be appointed for cause to take over the management of a firm in distress, their appointment in Chapter 11 is exceptional.

Recommendations in the Guide can be grouped along a broad spectrum of specificity that runs from broad statements of commercial norms to explicitly detailed language that is ready for enactment. The recommendations may be substantive, procedural or indeed conditional in nature. Conditional recommendations are predicated upon a particular procedure being enacted and specify that if one has this provision then it should have such and such content. For instance, according to Recommendation 151, where the insolvency law does not require a plan to be approved by all classes, it should address the treatment of those classes not voting to approve a plan that has been approved by other classes. Conditional recommendations give UNCITRAL ‘the capacity to acknowledge local contingencies and variations in an orderly way’.

The Guide also contains minimalism norms specifying that if there is to be a rule on a particular topic, or an exception to a rule, it should be kept to a minimum. For example, Recommendation 188 on secured claims provides that the:

- The insolvency law should specify that a secured claim should be satisfied from the encumbered asset in liquidation or pursuant to a reorganization plan, subject to claims that are superior in priority to the secured claim, if any. Claims superior in priority to secured claims should be minimized and clearly set forth in the insolvency law.

b. Standard setting by the World Bank including the Doing Business project

In 2000, the World Bank produced a background paper, ‘Building Effective Insolvency Systems: Toward Principles and Guidelines’. This paper led to the

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106 See the statement at p 162 of the commentary attached to the Legislative Guide: ‘In reorganization proceedings, there is no agreed approach on the extent to which displacement of the debtor is the most appropriate course of action and, where some level of displacement does occur, on the ongoing role that the debtor may perform and the manner in which that role is balanced with the roles of other participants.’

107 Section 1104 US Bankruptcy Code provides that a trustee can be appointed only for cause such as fraud, dishonesty or gross mismanagement and that large numbers of bondholders or shareholders are not enough.


109 Ibid at 503.
formulation of the Insolvency and Creditor Rights (ICR) Principles in 2001 and these principles have gone through various amendments and iterations with the most recent being in 2015.110

1.61 Since 2004, a team within the World Bank group have also produced the Doing Business reports and rankings which purport to measure a whole host of matters including ‘resolving insolvency’ and ‘getting credit’. The reports and rankings are based on a more sophisticated version of the ‘legal origins’ or ‘law matters’ thesis developed by four economists – La Porta, Lopez de Silanes, Shleifer and Vishny.111 These rankings also draw to a certain extent upon international standards in the field of insolvency and secured credit law that have been developed both by the World Bank itself and by UNCITRAL.

1.62 In determining the ‘Doing Business’ rankings, two factors are equally weighted though the second factor was only introduced into the Doing Business methodology in 2015.112 The first factor, and which has been part of the ‘resolving insolvency’ rankings since their inception, is the percentage recovery by secured creditors through restructuring, liquidation or debt enforcement proceedings. A hypothetical case study is posited and then likely recovery rates under the facts of this case study are calculated. The calculation takes into account whether the business emerges from the proceedings as a going concern or whether assets were sold piecemeal. Then the costs of the proceedings are deducted and, in line with international accounting practice, regard is also had to the value lost as a result of the money being tied up in insolvency proceedings for a particular period of time.113


112 See 2016 Doing Business report, accessed 4 February 2021 at https://www.doingbusiness.org/en/reports/global-reports/doing-business-2016 at p iv: ‘Since the first Doing Business report was published … the team has implemented a number of methodological improvements, expanding the coverage of regulatory areas measured and enhancing the relevance and the depth of the indicators. While initially the report was focused largely on measuring efficiency and the costs of compliance with business regulations, over the past two years there has been a systematic effort to capture different dimensions of quality in most indicator sets.’

3. CONFORMITY OF THE RESTRUCTURING DIRECTIVE

The recovery rate is taken as a measure of efficiency because time and cost are two important components whereas the second factor in its rankings – the strength of the insolvency framework index – is a proxy for quality because it measures how well insolvency laws accord with internationally recognised good practices. This second factor is made up of the aggregate of scores on an overall index that purports to measure and evaluate provisions on the commencement of proceedings, management of debtor’s assets, reorganisation procedures and creditors’ rights. Scores on the index range from 0–16, with the higher scores supposed to signify that particular insolvency laws are better designed for rehabilitating viable firms and liquidating non-viable ones.

In advancing the case for a new Restructuring Directive, the European Commission used as evidence the ranking of EU countries on the World Bank Doing Business Resolving Insolvency framework. Reference was made to the fact that the Doing Business (DB) project ranks countries according to efficiency on a scale of 0–16 and then pointing out ‘The EU average is 11.6, which is 5% below the OECD average for high income countries.’

The DB ‘resolving insolvency’ scores are premised on a cluster of normative assumptions that some elements of insolvency law are better or more desirable than others. The assessment is relatively crude and depends largely on blunt all or nothing measures. It assumes that particular legislative solutions are superior to others and misses out subtlety and nuances in the laws of a particular country. The approach simply asks whether one specific rule does or does not exist in different countries and effectively disregards other legal solutions that achieve the same goal. In its justification for an EU-wide legislative instrument, the European Commission also referred to statistics in the Doing Business report on recovery rates in insolvency proceedings across EU Member States which it said varied widely.
World Bank indicators suggest that recovery rates vary between 30% and 90% in the EU. Recovery rates are higher in economies where restructuring is the most common insolvency proceeding: in such economies creditors can expect to recover 83% of their claims, against an average of 57% in liquidation procedures. The length of insolvency proceedings ranges from a few months to four years, with 14 Member States having procedures which last for two or more years.

1.66 Reliance on these statistics is questionable since the methodology used to determine the recovery rate seems highly contestable for at least three reasons. Firstly, the rate is seen as a function of the outcome, time and cost of insolvency proceedings in respect of a particular kind of local company. There is no attempt, however, to measure whether the hypothetical case study is broadly representative of the local economy or whether different outcomes and returns could be expected in relation to different types of enterprises or case studies. Secondly, calculation of the rate also depends essentially on the subjective views of questionnaire respondents on the returns to creditors in their particular countries. In most countries, there will not be any publicly available and accurate data on these matters. Thirdly, the recovery rate is based on the percentage recovery by secured creditors through restructuring, liquidation or debt enforcement proceedings. The focus in the rankings is also solely on returns to secured creditors and if the insolvency law in a particular country had redistributionist elements this would necessarily reduce the returns to secured creditors and, therefore, a country’s position in the rankings would fall.
preferential rights of employees in the next review of the Regulation. Depending on which, if any, policy option is adopted this may have the effect of worsening the position of EU countries in the rankings.

c. Chapter 11 of the US Bankruptcy Code

Chapter 11 has been hailed in enthusiastic terms by its supporters and as the model to which restructuring laws across the globe should aspire.\textsuperscript{122} For instance, the DB insolvency ranking criteria draw heavily from the US Bankruptcy Code and in particular, Chapter 11. Perhaps it is not surprising that the US scores a maximum 3 out of 3 on a restructuring or reorganisation proceedings index as it is called. The relevant provisions here have three elements. The first element requires that the restructuring plan should be voted on only by the creditors whose rights are modified or affected by the plan. A score of 1 is given if this is the case; 0.5 if all creditors vote on the plan irrespective of the impact on their interests and 0 if either creditors do not vote on the plan or there is no regime for business restructuring. The second element requires that creditors entitled to vote on the plan should be divided into classes, that each class should vote separately and that creditors within the class should be treated equally. A score of 1 is only given when the voting procedure has these three features. The third element imports what in the US is referred to as the ‘no creditor worse off’ test, that is, dissenting creditors should receive as much under the restructuring plan as they would in liquidation.\textsuperscript{123} A score of 1 is given only if the relevant law has such a provision.

In general, the main features of Chapter 11 are as follows:

- The management of the company is not displaced in favour of an outside insolvency practitioner and the management itself can prepare a restructuring plan and submit the plan to the creditors.
- An officer may be appointed to monitor the debtor during the rehabilitation process, but the officer’s powers are not as far-reaching as those under a management-displacement regime.
- Moratorium exists to protect the company from its creditors.


\textsuperscript{123} US Bankruptcy Code section 1129(a)(7)(A)(i).
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- There is also a mechanism for the approval of a restructuring plan including ‘cram-down’ provisions under which a class of creditors, including secured creditors, can be forced to accept a restructuring plan against their wishes. This is the case if the court determines that there is at least one class of creditors who have accepted the plan and also if the court is of the view that the restructuring plan is feasible.
- There is provision for debtor-in-possession financing under which the company can obtain new funds either to continue its operations or to further the restructuring process. The providers of these new funds may enjoy ‘super-priority’ ahead of other creditors if existing creditors are deemed by the court to be adequately protected.

1.69 These elements are all found to a greater or lesser extent in the Restructuring Directive. There are undoubtedly strong similarities between the Directive and Chapter 11, most notably in relation to the debtor-in-possession norm; the provision for a stay on claims against the debtor to facilitate the restructuring process; the treatment of so-called ‘executory contracts’ which are contracts not yet fully performed by the relevant parties; the conditions for getting a restructuring plan approved; and the protection for new money finance. Nevertheless, there are also differences in detail between the Directive and Chapter 11 in each of these areas. For instance, while the Chapter 11 stay is automatic in its effects and global in its reach, the stay proposed under the Directive is discretionary. Chapter 11 also contains a much more extensive new finance regime than that under the Directive.

1.70 There are also a number of general comments, however, that are appropriate about using Chapter 11 as a model and how it might impact on the success of the Restructuring Directive. Firstly, Chapter 11 in something like its present form became part of the US Bankruptcy Code in 1978 though there were earlier precedents. Since then Chapter 11 has undergone a mini-metamorphosis with now much more of a market orientation to the process. There is a greater emphasis on whole or partial sale of the business assets on a going-concern basis rather than creditors and shareholders coming together under the umbrella of Chapter 11 and working out a restructuring plan. While

124 On the worldwide effect of the US automatic stay see In re Nortel Networks Inc (2011) 669 F3d 128.
125 COM (2016) 723 final Articles 6 and 7.
the figures are disputed, it has been estimated that ‘roughly two-thirds of all large bankruptcy outcomes involve a sale of the firm, rather than a traditional negotiated reorganization in which debt is converted to equity through the reorganization plan’. Part of the difficulties in working out statistics is that a company may undergo dramatic changes during the Chapter 11 process. Outcomes are often imprecise, difficult to measure and may be assigned potentially to more than one category. Companies may shrink in size, be split into multiple businesses, sell their businesses to new owners, discharge their managers, change their names, and fundamentally change the nature of their businesses. One or more businesses may survive after a bankruptcy, but it may nevertheless be difficult to say whether that survivor is the bankrupt company, a company that acquired the bankrupt company, or a company that acquired elements of the bankrupt company.

It should be noted that ‘restructuring’ as envisaged in the final version of the Directive now encompasses going-concern sales as well as restructurings as conceived of in the traditional sense. Restructuring includes ‘changing the composition, conditions or structure of a debtor’s assets and liabilities or any part of the debtor’s capital structure, such as sales of assets or parts of the business and, where so provided under national law, the sale of the business as a going-concern’.

Secondly, the business and financing landscape has also changed fundamentally since Chapter 11 was enacted and this has prompted calls for its revision. In short, there has been more expanded use of secured credit, growth in distressed-debt markets as well as other factors that have impacted on the effectiveness of the current law. Leading commentators have observed:

We have a new form of chapter 11 emerging in the courts. Having invented the DIP (debtor-in-possession), American lawyers are now creating the SPIP (secured-party-in-possession). More and more chapter 11 cases seem to be no more than vehicles through which secured parties may enjoy their Article 9 rights under the umbrella, and the protective shield, of the bankruptcy law.

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Insolvency and restructuring law in the US may undergo significant change in the next few years. One of the influential actors in the reform process – the American Bankruptcy Institute (ABI) – produced a comprehensive report in 2014\textsuperscript{132} detailing a proposed list of changes to Chapter 11.

The reforms were proposed with a view to achieving a better balance between the effective restructuring of business debtors, the preservation and expansion of employment, and the maximisation of asset values for the benefit of all creditors and stakeholders.\textsuperscript{133} But the nature of the political process in the US is such that these changes are unlikely to be enacted in the very near future.\textsuperscript{134}

The US, however, has recently enacted and implemented the Small Business Debtor Reorganization Act 2019. The Act adopts and modifies certain aspects of the ABI Commission report. It aims to make small business bankruptcies faster and less expensive by creating a new subchapter in Chapter 11 that is specific to small businesses. It streamlines small business restructurings and removes procedural burdens and costs associated with typical corporate restructurings. In particular, it removes the requirement that holders of ‘equity’ as distinct from debt in the small business debtor have to provide new value to retain their equity interest in the debtor without paying creditors in full.

Thirdly, Member States must be sensitive to the fact that solutions which may work well in one country may not work so well in other countries where the


\textsuperscript{133} For other criticisms of Chapter 11 see e.g. DA Skeel, ‘Rethinking the Line between Corporate Law and Corporate Bankruptcy’ (1994) 72 \textit{Texas Law Review} 471 at p 535: ‘Like an antitakeover device, bankruptcy can impair the market’s ability to discipline managers because it may substitute reorganization procedures for market mechanisms that would otherwise lead to the ouster of managers outside of bankruptcy.’ But this criticism has largely fallen away with new forms of market governance in US bankruptcy cases – see DA Baird and RK Rasmussen, ‘The End of Bankruptcy’ (2002) 55 \textit{Stanford Law Review} 751; ‘Private Debt and the Missing Lever of Corporate Governance’ (2006) 154 \textit{University of Pennsylvania Law Review} 1209; B Adler, V Capkun and L Weiss, ‘Value Destruction in the New Era of Chapter 11’ (2013) 29 \textit{Journal of Law, Economics, and Organization} 461.

\textsuperscript{134} For detailed criticism of the report by the Loan Syndications and Trading Association (LSTA) see ‘The Trouble with Unneeded Bankruptcy Reform: The LSTA’s Response to the ABI Commission Report’ (October 2015) at p 9: ‘If adopted, these reforms risk disrupting the operation of a bankruptcy system that has served the nation very well—aiding in the economic recovery from the Great Recession—and that has become the envy of the world. They also threaten to increase the cost of credit to both performing and distressed businesses, which will in turn hurt the very businesses that the proposals are designed to help.’
balance of interests is very different. The Directive contains a central underlying philosophy of promoting business rescue but it is also committed to the balancing of the interests of the different economic actors within the restructuring and insolvency process. The concept of balance is fundamentally important. UNCITRAL, for instance, has stressed that a desirable legal framework should ‘(a) Provide certainty in the market to promote economic stability and growth; (b) Maximize value of assets; (c) Strike a balance between liquidation and reorganization; (d) Ensure equitable treatment of similarly situated creditors ...’. For reasons of history, culture and experience and because of pressure group politics, the balance may have to be struck in different ways in different countries. For instance, the importance of the local in the global context has been acknowledged by the Insolvency Law Review Committee in Singapore. Singapore is seeking to position itself as a global restructuring hub – certainly in the Asia-Pacific region – by enacting modern laws and attracting international business. Nevertheless, the Committee recognised that while Chapter 11 has proved durable and successful in the US, it would be inappropriate to attempt to replicate it in Singapore where the local economic and social conditions were very different.

In a business restructuring context, parties bargain in the shadow of the framework provided by liquidation law. The law may create a context that is conducive to business restructuring, inter alia, by allowing majority decisions and also by facilitating the continuation of the enterprise during a period of ongoing negotiations. Nevertheless, the parties must consider the alternatives if the negotiations fail. Liquidation and debt enforcement law provides these alternatives and liquidation law is ultimately a distributional exercise – ‘who gets paid what'. Liquidation law reflects distributional norms and interest group politics rather than being purely an exercise in abstract economic

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136 See UNCITRAL Legislative Guide on Insolvency Recommendation 1.
137 See generally JM Garrido, ‘No Two Snowflakes Are the Same: The Distributional Question in International Bankruptcies’ (2011) 46 Texas International Law Journal 459 at pp 460–61 stating that ‘there are no two priority systems that are identical, and that harmonization or unification of the law in this area is extremely unlikely to happen’.
efficiency. Provisions in national insolvency law giving priority to certain categories of claim express the political bargains that have been reached in that particular country.

Fourthly, the Directive still leaves a considerable degree of flexibility for Member States and can be characterised as more minimum rather than maximum harmonisation. The Commission has referred to the Directive as ‘establishing a minimum harmonised framework covering a number of key aspects … conducive to effectively achieving the policy objectives in the areas of restructuring and insolvency, which are highly regulated at the national level’. Member States are not necessarily obliged to put in place any new legislative measures. They can claim any existing statutory regime they may have which is in conformity with the Directive. It is also stated that such frameworks may consist of one or more procedures or measures.

Fifthly, if politics is the ultimate dynamic that pushed the Restructuring Directive up the European legislative agenda, it also appears to have manifested itself in the minutiae of policy formation. Political compromise is at the heart of the Directive provisions. These are no strangers either in US Chapter 11 bankruptcy and restructuring. The restructurings of the giant auto manufacturers, General Motors (GM) and Chrysler, with the financing assistance and goodwill of both the US and Canadian governments are an example in point. New finance was provided in abundance to facilitate the restructurings.

The political context of restructuring and insolvency law has been hotly contested in the US. On one side of the coin are those who argue that ‘once all stakeholders’ interests are taken into account, if survival is achievable, survival

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141 See SWD (2016) 357 final at p 51.
142 Article 34 states that Member States shall adopt and publish, within 2 years from the date of entry into force of this Directive, the laws, regulations and administrative provisions necessary to comply with this Directive. They then have to communicate to the Commission the text of those provisions.
143 On the broader dimensions of insolvency law see generally F Mucciarelli, ‘Not Just Efficiency: Insolvency Law in the EU and its Political Dimension’ (2013) 14 EOBOR 175.
is virtually always economically preferable to liquidation'. These commentators point to the large economic and social costs that company failure places on employees, suppliers, customers and communities. On the other hand, it has been suggested that the ‘paradigmatic firm is a restaurant in a large city. When the restaurant closes, workers lose their jobs, but they can find work elsewhere. A new restaurant or another firm can move into the space, and life goes on.’ On this side of the theoretical divide, it is argued that if employment preservation is seen as an independent policy of bankruptcy law, then it has the potential of undermining the key role of insolvency law in facilitating economic growth. In a free-market or entrepreneurial economy, there have to be consequences associated with unsuccessful risk taking, and bankruptcy law should not distort incentives and interfere with market mechanisms for monitoring and disciplining.

These debates have been played out in the context of the restructurings of the huge auto manufacturers, GM and Chrysler. The US government provided new finance to facilitate a sale of the enterprises to restructured entities. Critics argue that the US government:

may well have saved jobs, but only in the Orwellian universe where it make sense to punish the more efficient because they produce using fewer jobs than the less efficient ... To say that the government ‘saved jobs’ overall both ignores the repercussions felt by other manufacturers ... as well as to take credit for the jobs that are saved by propping up the least efficient producer!

Notwithstanding this, and while the US government may have exited its investments in the restructured GM and Chrysler entities at a net financial loss, an overall cost–benefit assessment has to take into account the enormous social cost and dislocation associated with the closure of these entities. This would have caused an asymmetric shock in a particular region of the US with devastation of the local tax base and a perceived need to provide unemployment relief, training, assistance and relocation packages as well as other

transfer payments. The leading bankruptcy law professor and influential US Senator Elizabeth Warren has commented in an analogous context: ‘Business closings affect employees who will lose jobs, taxing authorities that will lose rateable property, suppliers that will lose customers, nearby property owners who will lose beneficial neighbours, and current customers who must go elsewhere.’

1.82 The global financial crisis has brought about shocks of an asymmetric nature in the EU. These have produced political instability and exacerbated difficulties in particular countries. The potential implications of restructuring law for employment therefore cannot be ignored in an EU context. Promoting restructuring law reform at the EU level that fosters growth and, even indirectly, facilitates employment, seems not only to be worthwhile but also a political imperative.

1.83 In another period of time, however, it appears that US Chapter 11 filings were used by companies to rewrite collective bargaining agreements with employee unions. This was a tactic in heavily unionised sectors of the economy such as the airline industry. Perhaps conscious of this history, employee rights have now been specifically factored into the European restructuring proposal. ‘Trade Unions’ representatives warned against the moral hazard risk that business may use restructuring frameworks strategically to reduce their liabilities towards workers.’ A number of directives currently guarantee information and consultation rights before restructuring and/or collective redundancies and the restructuring proposal is stated to be without prejudice to these. Under the proposal there may be a stay of enforcement actions following the commencement of restructuring proceedings. There is, however, in principle relief from the stay with respect to workers’ outstanding claims as defined in Directive 2008/94/EC. A stay in relation to such claims is only permissible for the amounts and during the period that Member States guarantee the payment of such claims by other means.

152 See the comment by B Carruthers and T Halliday, Rescuing Business: The Making of Corporate Bankruptcy Law in England and the United States (Oxford, Clarendon Press 1998) at p 266: ‘[S]olvent firms have filed for Chapter 11 bankruptcy to take advantage of the considerable powers incumbent managers have to remake the corporation, undo its commitments, and reduce its obligations … In many cases, the reorganizing firm was not insolvent, and may in fact have been performing rather well.’
153 SWD (2016) 357 final at p 16.
154 Articles 6 and 7.
155 Article 6(3).
In a proposal designed ultimately to promote jobs and economic growth, it clearly makes sense to allay concerns by employee representatives about some aspects of the proposal. Nevertheless, despite this concern for employee interests, employees may be adversely affected by the application of the cross-class creditor cram-down rules in Article 11 of the proposal. While employees may constitute a separate class under the class formation rules, there is no requirement of class unanimity before a restructuring plan can be approved by a court or administrative authority. A whole class or classes of creditors, including an employee class, may be crammed down if certain conditions are satisfied.

Sixthly, it is important to note the limitations of business restructuring law. Not all enterprises or indeed ‘businesses’ can be saved and, indeed, it must be said that definitions and statistical interpretations of business success or failure vary widely. This issue has provoked a lively debate particularly in the US where the dockets in all bankruptcy/insolvency cases filed are publicly accessible via the Public Access to Court Electronic Records (PACER) system. This facilitates the production of a range of statistical information on Chapter 11 cases by academic and private providers. One of the best known of these is the UCLA-LoPucki Bankruptcy Research Database which provides information on the outcomes in large cases. The available statistics may be interpreted in different ways and this is acknowledged by the team behind the database in a recent study, ‘Bankruptcy Survival’. The study suggests that about 70 per cent of large, public companies in the US that seek to remain in business through bankruptcy reorganisation succeed whereas the assets of the other 30 per cent are absorbed into other businesses.

156 Article 9(2).
157 Article 9(4).
159 For US consideration of this see National Bankruptcy Review Commission, Bankruptcy: The Next Twenty Years (E Warren, Reporter, 1997), accessed 26 January 2021 at http://govinfo.library.unt.edu/nbrc/ acknowledging at p 611 that reasonable people differ about how to define ‘success’ in Chapter 11 cases: ‘Some argue that a Chapter 11 case in which no plan is confirmed should be considered successful where the case produces an orderly sale of assets or a negotiated solution without a formal plan. Creditors may define success in terms of distribution amounts or in terms of preserving future dealings with the debtor. The debtor, on the other hand, may define success in terms of job preservation, enhancement of going-concern value, or future returns to equity. The public may define success in terms of overall fairness.’
162 For a somewhat different analysis of the data see, e.g., K Ayotte and D Skeel, ‘Bankruptcy or Bailouts’ (2010) 35 Journal of Corporate Law 469 at p 477: ‘[R]oughly two-thirds of all large bankruptcy outcomes involve a sale of the firm, rather than a traditional negotiated reorganization in which debt is converted to equity through the reorganization plan.’
Chapter 1 INTRODUCTION

1.86 The study recognises, however, that it is difficult to define the concept of bankruptcy survival since companies may undergo tumultuous changes during bankruptcy.

They may shrink in size, be split into multiple businesses, sell their businesses to new owners, discharge their managers, change their names, and fundamentally change the nature of their businesses. One or more businesses may survive after a bankruptcy, but it may nevertheless be difficult to say whether that survivor is the bankrupt company, a company that acquired the bankrupt company, or a company that acquired elements of the bankrupt company.\(^\text{163}\)

1.87 The LoPucki study tries to navigate around these difficulties by regarding the company as the web of relationships among employees and with outsiders and firm assets. If the structure of those relationships survives and remains distinguishable from the company’s owner, then the company is taken as surviving. The GM case is given as an example because, after the bankruptcy filing, the valuable part of the company’s business including its name, its managers and employees, were transferred to a new company formed to purchase them. The old company remained in bankruptcy but did not carry any business and changed its name to Motors Liquidation Company. GM is regarded as surviving bankruptcy because the sale of the web of relationships constituting the company is regarded as the sale of the company.

4. CONCLUSION

1.88 The former European Commission President, Jean-Claude Juncker, said on taking office that his first priority was to put growth and jobs at the centre of the European policy agenda.\(^\text{164}\) Addressing insolvency and business failures with the Restructuring Directive contributes to this policy because fewer insolvencies should mean that workers keep their jobs and businesses can contribute to growth across the EU. Reducing the number of insolvencies will see creditors and other stakeholders incurring fewer losses and enable them to assist in the growth process. It should also mean less dislocation in local and national communities throughout the EU. Reducing the divergence of national insolvency frameworks could also assist growth by contributing to the emergence of pan-European equity and debt markets. This would reduce uncertainty for investors who would otherwise have to assess investment risks on a country-by-country basis.

\(^{163}\) Ibid at p 979.

There is no guarantee, however, that implementation of the Directive will necessarily lead to an economic upturn165 though it may have the effect of boosting the position of the EU countries in the World Bank ‘resolving insolvency’ rankings. It is the case, however – despite suggestions from the European Commission to the contrary – that EU countries already score pretty well on these rankings; certainly on the 2020 ranking with Finland at number 1 and Germany at number 3. In the latter rankings, the majority of the top 20 spots are occupied by EU countries and the other top performers are generally First World developed economies.166

Perhaps the strongest example of the lack of correlation between economic success and World Bank ranking position is China. China has scored relatively poorly on the World Bank rankings including for ‘resolving insolvency’ and ‘getting credit’167 but has done enormously well economically lifting hundreds of millions of people out of poverty, though it faces new challenges as its economy enters a more mature phase. The Chinese experience tends to show that legal changes must be sensitive to local conditions and take account of different implementing environments. There are choices, or a set of choices, to be made between means and ends and that the relationship between means and ends is contingent and uncertain. To date, the development of the financial system in China has had uniquely Chinese characteristics.168 China’s singular journey suggests the need to avoid simplistic conclusions that certain consequences will inevitably follow from certain formal changes. It also suggests the need for a continuous process of adaptation and development; learning sensitively from experience and responding appropriately to local conditions.169

165 For a somewhat sceptical perspective on the merits of restructuring versus liquidation see D Baird and R Rasmussen, ‘The End of Bankruptcy’ (2002) 55 Stanford Law Review 751 at p 758: ‘We have a going-concern surplus (the thing the law of corporate reorganizations exists to preserve) only to the extent that there are assets that are worth more if located within an existing firm. If all the assets can be used as well elsewhere, the firm has no value as a going concern.’


167 In the 2017 rankings, for instance, it is 53rd for ‘resolving insolvency’ and 62nd for ‘getting credit’.


This chapter has already noted the limitations of business restructuring law. The law can create an environment that facilitates negotiations on financial deleveraging; the adjustment of debts and other ongoing obligations. But it cannot mend a bad business model. If a particular company is exclusively committed to the manufacture or supply of a product for which there is no market then the law cannot fix this. Having an efficient liquidation law that facilitates the move of assets away from inefficient enterprises may contribute more significantly to the overall health of the economy. But the Directive should also be able to assist in this regard since it includes more general provisions designed to enhance the efficiency of insolvency as well as restructuring and second chance procedures.

One thing that the Directive will not lead to, however, is a pan-European, more or less fully harmonised restructuring and insolvency law. The text of the Directive finally agreed upon is in many ways a compromise and it leaves Member States with ample room for different options in the implementation process. It has been estimated that the Directive contains at least 70 regulatory options for Member States. It remains to be seen whether the Directive will lead to more regulatory competition across Europe or whether restructuring options in certain States prove popular for companies incorporated in other EU Member States.

