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Subject:	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 - Policy debate

I. INTRODUCTION

The Justice and Home Affairs Council (the 'Council') on 8 and 9 June 2017 held a first policy debate on the proposed Directive and, on that occasion, endorsed a set of principles on some key issues for future work.¹

¹ See document 9316/17 JUSTCIV 112 EJUSTICE 65 ECOFIN 418 COMPET 415 EMPL 312 SOC 398 CODEC 833

In view of the discussions held by the Working Party since July 2017, the Presidency is of the opinion that it is necessary to have a policy debate in the Council to make further progress at Working Party level. The basic principles and the issues needing a certain degree of political guidance are set out in part II of this note. The Annex to this note provides further background to these basic principles.

II. BASIC PRINCIPLES AND POLITICAL GUIDELINES FOR FUTURE WORK

A. Viability of the debtor

The Council is invited to discuss whether they can agree to extending flexibility for the Member States by providing them with an option to introduce or maintain a viability test under national law, provided that the assessment has the purpose to exclude debtors with no prospect for viability and can be carried out without detriment to the debtor's assets.

Justification

Discussions at the technical level have shown that views on the viability of the debtor are quite divergent. Some Member States are of the opinion that granting access to a preventive restructuring framework or to a stay of individual enforcement actions to non-viable debtors would be detrimental to the debtor's assets and thus jeopardise the interests of creditors. Other Member States believe that granting unconditional access to the preventive restructuring framework and the stay of individual enforcement actions in all cases would incentivise the debtor to try to rescue their business at an early stage. The Presidency believes that the suggested guideline could therefore serve as a potential compromise between the diverging views. The reference "without detriment to the debtor's assets" does not exclude the possibility to require the debtor to prove its viability at its own cost.

B. Cross-class cram-down

The Council is invited to agree on the principle that, where there is more than one class of affected parties participating in the adoption of the restructuring plan and the required majority is not reached in one or more voting classes of affected parties, the restructuring plan may still be confirmed by a judicial or administrative authority provided that the requirements for such cross-class cram-down, as agreed during future discussions at technical level, are met. This is without prejudice to the outcome of the future discussion on class formation at technical level.

Justification

A majority of Member States acknowledges the need for a mechanism which allows the confirmation of a restructuring plan by a judicial or administrative authority even when there are dissenting voting classes, i.e. a restructuring plan is not supported by the required majority in one or more classes of affected parties, provided that certain conditions are fulfilled. At the same time, there are Member States which have a cautious approach to such a mechanism because it is something new and unknown in their legal systems. In order to advance the work at the technical level, the Presidency therefore needs guidance as to whether the proposed principle should serve as a basis for the future work.

C. Second chance for honest entrepreneurs

The Council is invited to discuss whether they can agree that there should be a harmonised discharge period of up to three years subject to limitations in cases where such a discharge or discharge period is not deemed to be appropriate.

Justification

Member States generally support the principle of giving honest entrepreneurs a second chance by granting them a full discharge of debts and a cancellation of any disqualifications linked to the insolvency of the debtor after a maximum period of time. This, however, is subject to the condition that sufficient safeguards and limitations are put in place where appropriate.

III. CONCLUSION

The Presidency invites the Council (Justice and Home Affairs) to hold a policy debate on the principles set out in Part II of this note as general guidance for the future work on the proposed Directive.

BACKGROUND INFORMATION

A. Viability of the debtor

The proposed Directive introduces an obligation for Member States to ensure that, where there is a likelihood of insolvency, debtors have access to a preventive restructuring framework that enables them to restructure their debts or business and to benefit from a stay of individual enforcement actions if, and to the extent that, such a stay is necessary to support the negotiation of a restructuring plan. The discussions so far in the Working Party have shown wide support for the approach of providing debtors with access to such a framework and a stay of individual enforcement actions as one of the tools to help rescue them from financial collapse.

However, a number of Member States have expressed concerns that allowing access to such a preventive restructuring framework or to a stay of individual enforcement actions to non-viable debtors might have a detrimental effect on the debtor's remaining assets and thus jeopardise the interests of creditors. Therefore, those Member States argue that a viability test of the debtor should be introduced as a precondition for granting access to the preventive restructuring framework or for granting a stay of individual enforcement actions in order to ensure the balance between the interests of the debtor and those of the creditors.

At the same time, other Member States are in favour of granting a debtor unconditional access to the preventive restructuring framework and the stay of individual enforcement actions, in order to incentivise the debtor to try to rescue their business at an early stage.

A compromise between these two different systems could be reached by giving the Member States the option to introduce or maintain a viability test under national law, provided that the assessment of the debtor's viability can be carried out without detriment to the debtor's assets.

B. Cross-class cram-down mechanism

According to the proposed Directive, a restructuring plan should always be deemed adopted or confirmed if the required majority of the affected parties in each class support it. The cross-class cram-down mechanism can be used when a restructuring plan is not supported by the required majority in each class of affected parties, leading to a dissenting voting class.

The cross-class cram-down mechanism is subject to a number of minimum harmonised requirements to ensure that the rights of the parties involved are appropriately protected. This means that the plan must be supported by at least one class of affected creditors, and dissenting voting classes must not be unfairly prejudiced under the proposed plan. Member States also have the option of increasing the minimum number of classes required to support the plan. In the case of a cross-class cram-down, the restructuring plan must always be confirmed by a judicial or administrative authority.

The principle of a cross-class cram-down complements the possibility of a successful restructuring by limiting the possibilities for affected parties without an interest in the restructuring to block the plan. The Member States generally acknowledge the need for such a mechanism, but a number of delegations question the proposed use of an absolute priority rule among the requirements. In addition, although there are Member States that already have the proposed mechanism in place in their national systems, there are others to which this concept is new.

Despite the fact that there seems to be support for this principle among the Member States, there are aspects in the proposed Directive that are new and unknown to some Member States. If such a principle is introduced at EU level, more flexibility is needed to allow the Member States to accommodate the principle appropriately to national legislations.

The degree and content of harmonised minimum rules on the adoption and confirmation of restructuring plans should be further discussed at technical level, and the technical work should, *inter alia*, focus on the formation of classes and the requirements of a cross-class cram-down (including the nature of those requirements).

C. Second chance for honest entrepreneurs

One of the key objectives of the proposed Directive is to enhance the possibility for a second chance for entrepreneurs within the EU. In this regard, the proposed Directive introduces an obligation for the Member States to provide a possibility for insolvent entrepreneurs to be fully discharged from their debts within a period defined by national law, which may not be longer than three years. Additionally, any disqualifications which are connected to the entrepreneur's insolvency should cease to have effect at the end of the discharge period at the latest.

In order to avoid abuse of the discharge procedure, the proposed Directive allows for the Member States to derogate from the abovementioned obligation in certain well-defined cases, where such a discharge or discharge period is not deemed appropriate.

Discussions have shown that the Member States generally support the principle of granting a debtor a full discharge of debts and a cancellation of any disqualifications linked to the insolvency of the debtor after a maximum period of time, provided that the debtor has gone through an insolvency procedure. This is, of course, subject to the condition that sufficient safeguards and limitations are put in place where appropriate. Further discussions at technical level are still needed to develop these safeguards and limitations.