Articles

Prof. Dr. Heinz Vallender, WP Michael Thierhoff, RA Daniel F. Fritz

Schemes for Everybody? Retailers still convincing Consumers? More equal than others?

Report about the 3. European Insolvency and Restructuring Congress, Brussels 22 – 23 May 2014, jointly organized by the ARGE Insolvenzrecht und Sanierung of the DAV and INSOLAD Vereniging Insolventierecht Advocaten

For the third time more than 120 European experts in insolvency law and restructuring gathered in Brussel to hear about the most recent topics in European insolvency law in the format of the "EIRC". This report gives a short impression about this event, in particular about two of its five workshops, the panel discussions and presentations, but is only giving a little taste of the intense and lively discussions the participants enjoyed at this occasion.

Harmonization and Distress – The first morning session

After warm welcoming words by Dr. Martin Prager, Chairman of the German Bar Associatiońs Section on Insolvency Law and Restructuring and Robert van Galen, President INSOLAD, the audience learned from the key note speak given by Michou Paraskevi, Director for Civil Justic, DG Justice, European Commission about the political backgrounds and key issues of the European Commissions "New approach to business failure and insolvency" and the status of the reform of the European Insolvency Regulation. The following presentation by Prof. Dr. Sweder van Wijnbergen (University of Amsterdam) gave some new insights and perspectives on the issues we are facing as not only banks but whole economies are now in distress.

After these presentations the morning session was completed by a detailed presentation from Mihaela Carpus-Carcea, Legislative Officer, DG Justice, European Commission, covering the new topic of harmonization of European insolvency law on national level. It was made clear that this new harmonization approach is not, yet (!) aimed at harmonization of the whole and in particular very different insolvency regimes of the individual member states, but for the time being and as a starter the general idea behind the European Commissiońs "New approach to business failure and insolvency". Here, the Commission offers now the outline and guidance for a new restructuring concept. Some may see it as a new tool, for early restructuring or as a pre-insolvency proceedings, in any case with lesser court involvement but still aimed to overcome the insolvency of an entrepreneur or a company within the framework of an insolvency plan. This hot topic led to a very lively discussion, chaired by Robert van Galen, where some participants doubted the necessity of this approach at all whilst others

could not wait to have such a new restructuring tool at hands. Insofar, Ms. Carpus-Carcea made it very clear that from the Commissions standpoint it is a relevant disadvantage if member states (like Germany) do not provide a short and effective scheme for restructuring prior to, resp. with the goal to effectively avoid fully flagged insolvency proceedings.

Report from the Workshop: "Some are more equal than others – Which debts should not be discharged"

This workshop was dedicated to issues arising in insolvencies of natural persons, in particular to the discharge of debts.

There are notable differences in policy in a number of European states, as became clear in the course of workshop IV, in which the members of the Panel[1], representing the legal systems of Germany, Greece, the Republic of Ireland, the Netherlands, Poland and England & Wales, described the debts from which debtors in their respective jurisdictions might be released and those that survive bankruptcy proceedings. Some common trends in policy may be discerned, but still, in significant respects, some creditors are more equal than others in the different jurisdictions.

England

The exceptions to the debts/liabilities from which a bankrupt is not released may be summarised as the following:

- certain claims arising from orders made in family proceedings (s. 281(2)-(8) IA 1986);
- liability for student loans (s. 42 Higher Education Act 2004);
- liabilities arising from fraud/breach of trust;
- fines and other penalties, confiscation orders (in criminal and similar proceedings);
- certain damages claims (e.g. for negligence for personal injury);
- future tort claims (*Re T & N Ltd* [2005] EWHC 2870 (Ch);
- debts incurred or arising after the making of the bankruptcy order (s. 382(1) IA 1986).

Germany

Following a long debate about the claims that should be excluded from discharge the law has been changed and two categories of debts have been added to the list in relation to child maintenance and tax evasion. With effect from 1 July 2014 § 302 InsO provides for the exclusion of the following categories of liability:

1. Claims arising as a result of intentional tort or an intentional failure to fulfill maintenance and claims arising in connection with a final conviction for tax evasion. The creditor has to register the claim as such an obligation.
2. Fines, administrative fines and other financial obligations imposed as part of a sentence.
3. Liabilities arising from interest-free loans made to fund the costs of the insolvency proceedings.

---

1 The workshop was led by Prof. Dr. Heinz Vallender of Cologne; the members were Hildegard Allemand, Allemand & Kemperdick (Cologne), Dr Stephen Baister, chief bankruptcy registrar of the High Court of Justice (London), Pawe? Kuglarz, Wolf Theiss (Warsaw), Dr. Hans Mathijsen, Willems Advocaten & Rechtsanwälte NV (Amsterdam), Barry O'Neill, Eugene F Collins (Dublin) and Stathis Potamitis, Potamitiskris (Athens).

Netherlands

Debts which are excluded from bankruptcy under the Dutch Insolvency Code are the following:

Student loans (Article 299 a of the Dutch Insolvency Code) and fines, liabilities arising out of an obligation to repay illegally obtained profits and Court ordered obligation to pay damage recoveries to the victim of a crime committed by the debtor, *if claimed within a criminal trial* (article 358 Dutch Insolvency Code).

Greece

Greek law makes no provision for the bankruptcy of individuals who are not merchants: the Greek Insolvency Code applies only to trading debtors, that is to say individuals or other legal entities engaged in commercial activity. Non-merchant debtors seeking release from their indebtedness must rely on the Law for the Arrangement of Debts of over-indebted Natural Persons, which provides individuals with the opportunity of reaching a negotiated settlement with creditors by a scheme of arrangement under the supervision of the court. If a negotiated solution cannot be reached then the court may impose a scheme on the parties.

There are certain categories of debt which are not capable of release. They are as follows:

(a) Debts incurred within a year of presentation of the petition.
(b) Those arising from intentional tort presentation of the petition.
(c) Fines and court imposed penalties
(d) Taxes and levies of central government, municipalities, regional authorities and public law entities
(e) Social security contributions

Poland

According to the current consumer bankruptcy regulations, unsatisfied obligations of the bankrupt may be released under Art. 491 of the Bankruptcy and Reorganisation Law. Generally the debts of the bankrupt fall to be satisfied in the bankruptcy proceedings under the terms of the debt settlement plan. Liabilities which will not be satisfied after completion of the plan are released.

In order to obtain his release from unsatisfied obligations, the bankrupt must present a petition to the insolvency court. The court must fix a hearing on notice to all creditors affected by the debt settlement plan. The insolvency court decides which creditors and obligations will be released.

Certain liabilities specifically referred to in the Bankruptcy and Reorganisation Law are excluded from release. Such exclusions are, however, limited to only two types of liability:

- periodical liabilities such as rent or lease obligations, and
- obligations incurred after bankruptcy registration

A proposed new Art. 491 will give the insolvency courts more discretionary power regarding release, whilst not freeing the bankrupt from obligations that

were lawfully imposed on him/her e. g. due to crimes committed or unpaid alimony.

Ireland

The Republic of Ireland has arguably taken the most radical approach to the issue of debt discharge in bankruptcy.

In the Republic of Ireland, there is only one type of personal bankruptcy. There is no distinction between consumer insolvency and commercial insolvency. In principle, bankruptcy has the effect of releasing a debtor from all his debts and liabilities. The debtor's bankruptcy status ends after three years. However, the administration of the bankrupt's estate continues until all assets are sold.

An individual may also obtain a release from his debts by means of an individual insolvency arrangement. Individual insolvency arrangements were introduced into Ireland by the Personal Insolvency Act 2012. Certain debts are defined as "excluded debt". The terms of the arrangements may not contain any provisions which would release the debtor from an "excluded debt" or otherwise affect such a debt.

Excluded debts are:

(a) a liability arising out of a domestic support order;
(b) a liability arising out of damages awarded by a court in respect of personal injuries or wrongful death arising from the tort of the debtor;
(c) a debt or a liability arising out of a loan obtained through fraud, misappropriation, embezzlement or a fraudulent breach of trust;
(d) a debt or a liability arising by virtue of a court order made under the Proceeds of Crime Acts 1996 and 2005 or by virtue of a fine ordered to be paid by a court in respect of a criminal offence.

Conclusion

For rehabilitation it is important that as many as possible of the debtor's debts be included in the discharge. The more debts that are excluded from the effect of the discharge, the less effective the insolvency regime can be in achieving the debtor's rehabilitation and the many related goals outlined above in section. The reports on the legal situation in the different countries and the following discussion with the attendants of the workshop showed that there is a general awareness, that debt discharge is a very much needed practical solution to a very common problem for individuals in a society, where "overspending" is an important economic factor. It also showed that related to this provision there also is the awareness and fear, that the solution could be misused and that "dishonest" debtors could profit from it. This results in the provision of safeguards in form of discharge exclusion regulations in varying intensity but all relating to some kind of dishonest behaviour.

Report from the Workshop: "Struggling Retailers in the Era of the Internet 2.0"

This workshop led by lawyer Daniel F. Fritz, Speaker of the European Affairs Working Group of the German Bar Associations Section on Insolvency Law and Restructuring. In contrast to the other workshops and presentation this work-

shop was not aimed at debating legal topics but practical restructuring issues, here in the context with the retail industry now struggling with the effects of the new online era.

The panelists' presentations started with a general overview about the retail market and its current trends and position. Here, Robert Klingler, Roland Berger Strategy Consultants, asked the question, whether the old retail model is dying. According to his view this may not – yet – be the case, but looking at the non-food retail sector, selling goods to customers becomes more an online affair. Only the food market is still the domain of stationary offline retailers and the "old" names are still growing in this market. According to Robert Klingler the survival of retailers is mostly an affair of knowing the customer, the retailers want to reach. Here more and more variaties of customers are to be reached through multi channels including online, offline and stationary sales.

The next presentation was given by Malcolm MacAulay, Gordon Brothers Europe. He was highlighting the simple truth, that cash is king and knowing about the value of the retailer's stock is always the big question. Interesting examples were given, how precisely the liquidation value of stock can be estimated in general, whereas the value is always very much depending on the type of goods in particular. Referring to a spanish case, Malcolm MacAulay demonstrated, that a successful restructuring of a retailer is sometimes not only based on a fast–track insolvency, but on full scale operational restructuring. This approach may need its time and sufficient financing as key factors for successful turnaround.

Next panelist, Andrew McCallum from Alvarez & Marsal, demonstrated the quick ways for a financial restructuring using the scheme of arrangement and UK administration proceedings in retailer insolvencies. Here the audience learnt, that the schemes are indeed a legal tool more than over 140 years old, but only most recently used in restructurings. In addition, an insider view was given to the recent ATU case, where the "bad bank"-model was used in a retailer restructuring, insofar separating the good from the bad assets of this group and finally sending the bad assets in a quick administration proceeding, allowing the stores to operate outside insolvency.

Last but not least, panelist was Marcel Wind (Houthoff Buruma). He demonstrated how the already existing "old" dutch insolvency law can be used nowadays allowing for quick dutch type of "prepack" without any law reform. In recent dutch insolvency practice the simple fact, that the courts changed their mind said, is now allowing creditors to approach the court with their proposals for an independent administrator prior to the filing. This gives the intented administrator the possibility to inform himself about the key issues of the proceedings prior to and prepare for his actual appointment. Based on the Marlies Dekker case, Marcel Wind demonstrated, how a timely introduction of the insolvency administrator allowed to minimize the potential liquidation losses as under these new conditions the typical phase of orientation – sometimes losing time money – could be skipped.

The presentations were followed by lively discussions with regards to typical challenges of this industry and the benefits and downsides of the packaged insolvency in contrast to a continuation of the business and fully operational

restructuring within the frame work of an insolvency proceeding, e. g. in the case of Deutsche Woolworth, which ended in a successful transfer of the restructured business within the framework of a regular German insolvency proceedings.

Report from the Panel and Discussion: "Schemes for everybody, please! Upsides and downsides of preventive pre-insolvency procedures

The subject topic of was covered in a 50 minute panel discussion followed by a 30 minute plenary discussion on the topic. The panel was chaired by Michael Thierhoff from Germany, an accountant specialised in restructuring and insolvency. The two panellists were Gerhard Gispen, a lawyer, current director of INSOL International and insolvency practitioner from the Netherlands, and Stephen Taylor, an English consultant with a long record of experience in advising stakeholders in distressed situations, predominantly with a cross-border impact.

Michael Thierhoff opened the session by relating to the presentation and discussion of the day before by Mihaela Carpus-Carcea of the European Commission's recent EU Recommendation on a "New approach to business failure and insolvency" recommending the introduction of a pre-insolvency framework for restructuring in all of the EU Member States. When it comes to restructuring it is common with healthcare that the earlier is the better. This is widely accepted and as a consequence early out of court pre-insolvency restructuring arrangements are commonly encountered. Acknowledging this leaves the question open, whether consenting business businessmen do require guidance and support by the law. If the answer is yes, the proper checks and balances needed are essential. For a legal framework it is imperative to assure fairness and thus avoid the misuse by fraudsters.

Gerhard Gispen's presentation was focussing very much on the checks and balances and expressing a clear scepticism with regard to pre-insolvency restructurings. Reminding that the restructuring needs do predominantly aim at the rescue of the business rather than of the entrepreneur and that when doing so it is essential not to interfere with fair competition and to remember that in a world where rescue is easy and cheap the flipside of the coin would be an increase of the cost of capital in the markets at large. More specifically Mr Gispen made the point for the creditors whose rights also require broad respect. Their position should be focus of the mediator or supervisor appointed who in his view should have the power to initiate insolvency proceedings if necessary. The creditors should also be involved when it comes to appointing the supervisor and granting a stay for the debtor. The stay should be conditioned by the support of the major creditors, be supervised and subject to meeting a milestone plan. For a plan to be enforceable it requires to respect the rights of secured creditors in full and be seen in competition with alternative options. It was also of importance that the plan will be recognised across the EU in all Member States. Once approved a plan should be set aside in the event that the debtor does not adhere to it or proves to be dishonest. In a successful effort to provoke some controversy Mr. Gispen made the statement that truly honest entrepreneurs are indeed rare.

Stephen Taylor finally took over clearly promoting a sound pre-insolvency restructuring framework. Congratulating the EU Commission for the Recommendation he supported the encouragement of early restructurings, making the point that an early restructuring with the debtor in possession does have ample merits. Even if the managers do not fully understand all of their stakeholders concerns they understand the business and are best placed to preserve the value in the interest of all involved. An early arrangement with creditors is in the majority of cases a by far better solution than destruction and the flexibility of an out-of-court settlement is, not only for its speed, to be preferred over formal processes. In any event insolvency processes and their unavoidable resulting in significant collateral damage should be a last resort. With this in mind the good mediator should be assisted by a framework to convince both debtor and creditors to balance their individual goals in the interest of a greater good for all. With a view from a different angle he reminded creditors to be more diligent when assessing and appraising their exposure. Creditors should support good governance and clearly understand the full range of possibilities at their disposal and their impact.

The following lively discussion involved panellists and attendees alike. It was chaired by Daniel F. Fritz and Alice van der Schee. Major points of the discussion were around cost involved in debtor-in-possession proceedings as well as their acceptance by creditors. Another point of the discussion was securing fair competition. As one might expect the opinions voiced were far from being in agreement.

Reforms and Discussions – The second morning session

Besides the panel about preventive pre insolvency proceeding and the following discussion the remaining morning was dedicated to learn about the insolvency law reforms on the national levels in Germany (presented by Marie Luise Graf-Schlicker, Director General, Federal Ministry of Justice), from the Netherlands (presented by Ilona Wolffram-van Doorn, legal counsel, Ministry of Security and Justice) and from Poland (presented by lawyer Michal Barlowski). Ms. Luise Graf-Schlicker gave insights in the current German law reform, resp. the German Government's approach in relation to the insolvency of groups of companies and the idea to mutually enrich the reforms on the national and European level in this current hot topic of insolvency legislation. However, she made clear that at least Germany, just having introduced the new protective shield proceedings does not see the need for earlier restructuring proceedings. In contrast to this Ms. Wolfram-van Doorn was laying out that the Netherlands are actually working on such new law introducing a preventive pre-insolvency proceeding. Finally Mr. Barlowski explained the Polish model that will probably have to deal with five different types of restructuring proceedings in the future, encompassing a procedure on the confirmation of a settlement plan, an accelerated settlement procedure, a settlement procedure and a recovery procedure. Seeing how differently these three countries are dealing with insolvency laws one does not need to wonder that the Commission looking at this diversity may see a need for further harmonization in this area whereas others want to stick with their old shoes

Conclusion

In anyway it was the clear signal from this conference as mentioned and summarized in the closing words by Alice van der Schee (Vice-President Insolad) and Daniel F. Fritz, that the various regimes stay in competition with each other, the harmonization discussion is on the table and will hopefully combine the best ideas and practices from the EUs member states.