## EFFECTIVE INSOLVENCY FRAMEWORK WITHIN THE EU

ICAEW welcomes the opportunity to comment on the effective insolvency framework within the EU consultation published by the European Commission on 23 March a copy of which is available from this link.

This ICAEW publication contains a copy of our response of 14 June 2016 and our response reflects consultation with the Insolvency Committee which is a technical committee made up of Insolvency Practitioners working in large, medium and small practices. The Committee represents the views of ICAEW licence holders.

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ICAEW members operate across a wide range of areas in business, practice and the public sector. They provide financial expertise and guidance based on the highest professional, technical and ethical standards. They are trained to provide clarity and apply rigour, and so help create long-term sustainable economic value.



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## General comments

ICAEW responded to the European Commission's consultation on effective insolvency framework within the EU on 14 June 2016 through the Commission's on-line consultation questionnaire and a copy of that response is attached in the appendix to this publication.

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# Consultation on an effective insolvency framework within the EU

Fields marked with * are mandatory.

## Introduction

An appropriate insolvency framework is important for society at large and in particular for investors, creditors and debtors. It is an essential element of a good business environment and is therefore important for jobs and growth.

A good insolvency framework maximises the efficiency, predictability and effectiveness of insolvency proceedings. This makes it easier to trade, supports an effective credit system and ensures a favourable investment climate, in turn benefiting the wider economy.

Insolvency frameworks should provide a transparent, predictable and cost-effective set of rules that can be used to preserve and maximise the value of debtors' assets. The rules should make it possible, either to:

- save businesses (by restructuring the existing company or by selling it as a "going concern"); or
- make it easier to liquidate a company and its assets if that company has not prospect of survival.

Efficient insolvency rules could also help increase  the recovery rate of debts and avoid the build-up of non-performing loans in the financial system.

The Commission's Annual Growth Survey 2016 explicitly recognises the importance of *'well-functioning insolvency frameworks'*. These are *'crucial for investment decisions since they define rights of creditors and borrowers in the event of financial difficulties'*.

Conversely, inefficient and ineffective frameworks result in the discontinuation of viable businesses, lengthy procedures and a low rate of recovery. This often translates into significant problems for the Member States concerned and for the wider European economy. These problems may take the following forms:

- Unnecessary liquidation of viable businesses, resulting in a loss of productive capacity;
- *De facto* or *de jure* disqualification of failed entrepreneurs or the exclusion from economic life of indebted members of the public;
- Barriers to corporate lending and investment, including cross-border investment. Uncertainty or difficulties over realising value from distressed debt may be particularly pronounced in the case of cross-border lending and investments. This may increase the cost at which investors and creditors are willing to invest in or lend to cross-border borrowers.
- Difficulties for creditors in recovering value from distressed debt. This may contribute to persistently high levels of non-performing loans, which weigh on bank balance sheets and may constrain bank lending.

In the public consultation on a Capital Markets Union, insolvency laws were singled out as one of the key barriers preventing the integration of capital markets in the EU. Consultation respondents broadly agreed that both the inefficiency and divergence of insolvency laws make it harder for investors to assess credit risk, particularly in cross-border investments. Convergence of insolvency and restructuring proceedings would facilitate greater legal certainty for cross-border investors and encourage the timely restructuring of viable companies in financial distress [1].

**Focus on restructuring and a second chance:**

A clear and effective approach to debt restructuring can benefit both the borrowing and lending sides of the market. Businesses that are in temporary distress should be able to restructure and be saved if their business is viable. Member States' legal frameworks have a crucial role in creating the conditions for successful restructuring, whether within or outside formal insolvency proceedings.

To encourage entrepreneurial activity, entrepreneurs and managers of companies should not be stigmatised when honest business endeavours fail. Individuals should not be deterred from entrepreneurial activity or denied the opportunity for a 'second chance'. Similarly, managers of companies may benefit from clear rules on their disqualification over insolvency-related misconduct.

For consumers (i.e. individuals with debts of a non-professional nature), a possible second chance might give them the incentive to start consuming again and take up gainful employment without the stigma of insolvency burdening them for years on end.

This means that for individual debtors, whether entrepreneurs or consumers, the rules on how to discharge the remaining debt following bankruptcy are important. Any rules providing for debt discharge need to be carefully designed to prevent abuse and incentivise careful management of business debt from the outset.

As a result, in the Capital Markets Union Action Plan, the Commission announced its intention to propose a legislative initiative on business insolvency, including early restructuring and second chance. The legislative initiative seeks to address the most important barriers to the free flow of capital, building on national sets of rules that work well.

The Commission Communication '*Upgrading the Single Market: more opportunities for people and business*' states that the effects of a potential bankruptcy deter individuals from entrepreneurial activity. The prospect of a fresh start for bankrupt entrepreneurs encourages would-be entrepreneurs to start and scale-up new business activities. This creates a more beneficial environment for innovation.

**Helping creditors (banks) to recover value in the event of insolvency**

The Five Presidents' Report on '*Completing Europe's Economic and Monetary Union*' identified insolvency laws as a key component of Financial Union. An effective insolvency framework should also contribute to the efficient management of defaulting loans and reduce the accumulation of non-performing loans on banks' balance sheets.

This position on insolvency reform was set out in the Commission Communication '*Towards the Completion of the Banking Union*' of 24 November 2015. Efficient insolvency frameworks would increase recovery rates and improve pricing of non-performing loans in the interest of developing a secondary market. Such loans would not then remain on banks' balance sheets for protracted periods of time, debts could be at least partially recovered and debtors could have a fresh start.

The Commission has examined national insolvency regimes as part of the European Semester, the EU's economic governance framework. Lengthy, inefficient and costly insolvency proceedings in some Member States were found to be a contributing factor to insufficient post-crisis debt deleveraging in the private sector and exacerbating debt overhang.

**Objectives of this consultation**

This consultation asks about the key insolvency barriers. It focuses in particular on gathering views on:

- the efficient organisation of debt restructuring procedures;
- the rationale and the process for debt discharge for entrepreneurs (and its possible extension to consumers).

Beyond these two policy areas, the consultation also invites views on selected aspects of efficient and effective insolvency frameworks which may have particular importance for the Internal Market or the integration of capital markets. Such frameworks should help to maximise the value received by creditors, shareholders and other stakeholders.

The responses will be used to identify which aspects should form part of a legislative initiative [2] and other possible complementary action in this field. The responses will be taken into account alongside the results of an external economic study carried out on behalf of the Commission as well as other evidence and analysis. The results of the consultation are without prejudice to any potential future Commission proposal.

This consultation is run via the 'EU-Survey' online tool, which makes it easier to collect answers from the widest possible range of respondents. In addition to choosing from the pre-defined answers, respondents are encouraged to explain their views or add additional information or explanations in the free text boxes provided. Respondents can add additional information at the end of the consultation and/or can do so by clicking on the 'other' options and the boxes that follow. Alternatively, separate contributions can be sent to the dedicated mailbox.

[1] An Inception Impact Assessment which contains a detailed description of the problems found in this area, as well as the policy objectives and options for action is available on http://ec.europa.eu/smart-regulation/roadmaps/docs/2016_just_025_insolvency_en.pdf.
[2] The Commission Work Programme for 2016 announced a legislative initiative framing a new approach to business failure and insolvency.

## I. Information about you

This consultation is addressed to the broadest public possible, as it is important to get views and input from all interested parties and stakeholders.

*1. Please indicate your role for the purpose of this consultation

- ○ Private individual
- ○ Self-employed person
- ○ Company
- ○ Bank, credit institution, investment fund, financial institution
- ○ Judge
- ○ Insolvency practitioner
- ○ Other legal practitioner
- ○ Business adviser or business support organisation
- ○ Public authority
- ○ Academic
- ○ Think tank
- ◉ Other

*

**Please specify**

Professional body

**Name of your organisation** (if applicable)

ICAEW (Institute of Chartered Accountants of England and Wales)

**2. Is your organisation included in the Transparency Register?**

*(If your organisation is not registered, you can register here. You do not have to be registered to reply to this consultation.)*

- ◉ Yes
- ○ No

**If you are registered, please indicate your register ID Number:**

7719382720-34

*3. Have you had practical experience with insolvency proceedings?

- ◉ Yes
- ○ No

*In what capacity?

- ○ As a creditor
- ○ As an employee in the context of an insolvency proceeding of my employer
- ○ As an owner or director of an insolvent business
- ○ As an over-indebted private individual or consumer
- ○ As a judge
- ○ As an insolvency practitioner
- ○ As another kind of legal practitioner
- ○ As a business adviser or business support organisation
- ◉ Other

*

**Please specify**

ICAEW licenses insolvency practitioners in the UK and this response reflects the views of its Insolvency Committee which is made up of its insolvency practitioners, including practitioners with extensive experience of cross border insolvency.

*

**4. Please indicate the country where you are located:**

- ○ Austria
- ○ Belgium
- ○ Bulgaria
- ○ Cyprus
- ○ Czech Republic
- ○ Germany
- ○ Denmark
- ○ Estonia
- ○ Greece
- ○ Spain
- ○ Finland
- ○ France
- ○ Hungary
- ○ Croatia
- ○ Ireland
- ○ Italy
- ○ Lithuania
- ○ Luxembourg
- ○ Latvia
- ○ Malta
- ○ Netherlands
- ○ Poland
- ○ Portugal
- ○ Romania
- ○ Sweden
- ○ Slovenia
- ○ Slovak Republic
- ◉ United Kingdom
- ○ Non-EU country

**5. Please provide your contact information:**

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***6. Please indicate your preference over the publication of your response on the Commission's website:**

- (●) Under the name given: I consent to publication of all information in my contribution and I declare that none of it is subject to copyright restrictions that prevent publication.
- ( ) Anonymously: I consent to the publication of all information in my contribution, except my name/the name of my organisation and I declare that none of it is under copyright restrictions that prevent publication.
- ( ) Please keep my contribution confidential (it will not be published, but will be used internally within the Commission)

*Please note that regardless of the option chosen, your contribution may be subject to a request for access to documents under Regulation 1049/2001 on public access to European Parliament, Council and Commission documents. In this case, the request will be assessed against the conditions set out in the Regulation and in accordance with applicable data protection rules.*

## II. Questions

In general, an insolvency framework should ensure that viable businesses can be restructured and continue operating, while non-viable ones can be quickly liquidated. Over indebted individuals should also have access to insolvency proceedings and discharge provisions subject to certain conditions. Member States have in place different systems, some of which comply at least partially with these requirements and some of which do not. These differences may have an impact on the functioning of the internal market.

## 1. Scope

**1.1. Which measures should be taken to achieve an appropriate insolvency framework within the EU?** (choose all that apply)

- [ ] a) Preventive measures to enable the restructuring of viable businesses
- [ ] b) Measures to increase the recovery rates of debts in insolvency
- [ ] c) Measures to ensure the discharge of debts for entrepreneurs (individuals)
- [ ] d) Measures to ensure the discharge of debts for consumers
- [ ] e) Measures governing employees' rights in insolvency
- [ ] f) Measures ensuring the enforcement of debts
- [x] g) Other measures
- [ ] h) No opinion

**Please explain**

Please see our explanation regarding EU measures under question 1.2 below. As regards measures to be taken at a national level, a, b, c and f are all important considerations for an insolvency regime. It is somewhat difficult to see that discharge of consumer debt is a priority for business, but it is, of course, relevant for wider society and the distinction between consumers and entrepreneurs are likely to become increasingly blurred. Employees are of course relevant, but they could be treated as ordinary creditors so that an insolvency regime does not need to have specific employee measures. Employment laws do not always take due account of insolvency matters. For instance, the requirement to conduct meaningful consultation with employees before making redundancies (at least as implemented in the UK) does not take account of the practicalities involved in insolvency, where it may be necessary to make redundancies at short notice either to liquidate or to attempt to save the business.

**1.2. To what extent do the existing differences between the laws of the Member States in the areas mentioned below affect the functioning of the Internal Market?**

*(For example, differences affect the Internal Market when creditors or investors and debtors are located in different Member States and this has an impact on the recovery of debts, the legal certainty of transactions, the quantification of risks etc.)*

| | To a large extent | To a considerable extent | To some extent | Not at all | No opinion |
|---|---|---|---|---|---|
| a) Preventive measures to enable the restructuring of viable businesses | ○ | ○ | ◉ | ○ | ○ |
| b) Measures to increase the recovery rates of debts in insolvency | ○ | ○ | ◉ | ○ | ○ |
| c) Measures aimed to ensure the discharge of debts for entrepreneurs (individuals) | ○ | ○ | ◉ | ○ | ○ |
| d) Measures to ensure the discharge of debts for consumers | ○ | ○ | ○ | ◉ | ○ |
| e) Measures governing employees' rights in insolvency | ○ | ○ | ○ | ◉ | ○ |
| f) Measures ensuring the enforcement of debts | ○ | ○ | ◉ | ○ | ○ |
| g) Other measures | ○ | ○ | ○ | ○ | ◉ |

**Please explain**

The question presupposes that EU measures are required, but with limited exceptions we question this. The objectives of an insolvency regime, for instance regarding priority of creditors (including secured creditors or employees) may vary according to the political wishes of member state governments and principles of subsidiarity should be respected in this context. Insolvency laws and their place in society are dependent on other issues, such as property and employment laws and availability of skilled advisors and there is a risk that harmonization measures on insolvency will not adequately reflect this. The effectiveness and quality of regimes within the EU vary dramatically as is apparent from, for instance, World Bank. We support initiatives designed to help those with relatively poor regimes to reform their laws, for instance through Recommendations. If the Commission decides to proceed with formal harmonization measures, such as Directives, we believe that they should be designed to set minimum broad standards whilst allowing member states flexibility as to how those standards are applied in practice. The flexibility should be sufficient that those member states which already have relatively successful regimes would not be required to change them if they believe to do so would be prejudicial.

**1.3. To what extent do the measures mentioned below have an impact on the creation and operations of newly established companies?**

| | To a large extent | To a considerable extent | To some extent | Not at all | No opinion |
|---|---|---|---|---|---|
| a) Preventive measures to enable the restructuring of viable businesses | ○ | ○ | ◉ | ○ | ○ |
| b) Measures to increase the recovery rates of debts in insolvency | ○ | ○ | ◉ | ○ | ○ |
| c) Measures to ensure the discharge of debts for entrepreneurs (individuals) | ○ | ○ | ○ | ◉ | ○ |
| d) Measures governing employees' rights in insolvency | ○ | ○ | ○ | ◉ | ○ |
| e) Measures ensuring the enforcement of debts | ○ | ○ | ◉ | ○ | ○ |
| f) Other measures | ○ | ○ | ○ | ○ | ◉ |

**Please explain**

In the experience of our members, new businesses rarely pay much attention to matters of insolvency (except the regime on personal liability, for instance directors' liability) as their focus is on making the business a success. These issues may affect funding of a new business and it may be easier for businesses to obtain funding where the regime protects creditor rights. The main priority of a creditor is likely to be an assurance that it will be repaid, including effectiveness of security rights.

## 2. Saving viable businesses in difficulty

In general, an insolvency framework should ensure that viable businesses can be restructured and continue operating. However, the conditions under which a company is deemed viable and should be restructured or liquidated differ from Member State to Member State. In this consultation, the term ‘restructuring’ covers both restructuring as an existing company and the sale of a company as a going concern to another company. There is also a difference between the viability of a legal entity and that of a business contained within it or even spread across several legal entities.

The rules regulating restructuring procedures (including the contents of the restructuring plan and related procedural issues) have a crucial role in creating the conditions for successful restructuring, whether within or outside insolvency proceedings. There are major differences across Member States in the rules on the procedure for adopting a restructuring plan, including required majorities for its adoption and the rights of dissenting creditors.

Laws of Member States also differ on the standards applied by the courts when asking for a stay of individual enforcement actions (i.e. a suspension of the right to enforce a claim by a creditor against a debtor, also known as a ‘moratorium’) to be granted, when approving the plan and the possibility to challenge such approval. Moreover, under certain national insolvency frameworks, courts may have wide discretionary powers over the approval of the plan and possible changes to it, while under other laws these powers are rather more limited.

Rigid and impracticable rules may hinder the chances of adopting a restructuring plan. Restructuring viable businesses avoids unnecessary liquidation and thus helps safeguard the debtor’s assets as a going concern, maximising value for owners and shareholders as well as for creditors. An efficient business restructuring procedure may also give equity investors a chance to recover the value of their investment. At the same time, restructuring procedures must be safeguarded against misuse and depletion of the assets in the process.

There are also significant differences between the criteria for opening insolvency proceedings. In certain Member States, insolvency proceedings may be opened only for debtors that are already affected by financial difficulties or are already considered insolvent. In others, proceedings can be opened for solvent debtors that anticipate facing insolvency in the imminent future. Such proceedings do not have the character of informal pre-insolvency proceedings. Further differences may also be found in insolvency tests (liquidity test, balance sheet test, over-indebtedness test) and in the obligation for a debtor to file for the opening of insolvency proceedings when insolvency occurs.

In a company, directors exercise corporate powers which are generally balanced with duties of care prohibiting wrongful trading. Some Member States have certain obligations in place for directors in the period before insolvency occurs and impose liability for any harm caused by continuing to operate when it was either clear or should have been foreseen that insolvency could not be avoided. The rationale for such provisions is to create appropriate incentives for early action through the use of voluntary restructuring negotiations. It may also encourage directors to obtain competent professional advice when financial difficulties occur and thus avoid insolvency.

**GENERAL QUESTIONS**

**2.1. To what extent do existing differences between the laws of the Member States in the areas mentioned below affect the functioning of the Internal Market?**

*(For example, differences affect the Internal Market when creditors or investors and debtors are located in different Member States and this has an impact on the recovery of debts, the legal certainty of transactions, the quantification of risks etc.)*

| | To a large extent | To a considerable extent | To some extent | Not at all | No opinion |
|---|---|---|---|---|---|
| a) Measures to give access to a toolkit enabling fast restructuring | ○ | ○ | ◉ | ○ | ○ |
| b) Measures to ensure the assessment of a debtor's viability | ○ | ○ | ◉ | ○ | ○ |
| c) Measures to provide minimum standards in relation to the definition of insolvency | ○ | ○ | ◉ | ○ | ○ |
| d) Measures to lay down the duties of directors in companies in financial distress | ○ | ○ | ○ | ◉ | ○ |
| e) Measures to protect new financing given to companies that are being restructured | ◉ | ○ | ○ | ○ | ○ |
| f) Measures to clarify the position of shareholders of companies in insolvency or close to insolvency | ○ | ○ | ○ | ○ | ○ |
| g) Measures to promote assistance to financially distressed debtors | ○ | ○ | ○ | ◉ | ○ |
| h) Other measures | ○ | ○ | ○ | ○ | ◉ |

**Please specify which other measures in national laws affect the functioning of the Internal Market.**

Please see our comments regarding EU measures under question 1.2. The measures are generally ones that member states could be expected to take, although the position of ordinary shareholders on an insolvency is probably widely understood. As regards the single market, creditors will need to understand what their security rights are and, if they are to provide financing when a business is being restructured, any priorities that might protect new financing.

**2.2. What impact do the different types of measures mentioned below have on saving viable businesses?**

| | Very strong impact | Considerable impact | Little impact | No impact at all | No opinion |
|---|---|---|---|---|---|
| a) Measures to give access to a toolkit enabling fast restructuring | ◉ | ○ | ○ | ○ | ○ |
| b) Measures to ensure the assessment of the viability of a debtor | ○ | ◉ | ○ | ○ | ○ |
| c) Measures to provide minimum standards in relation to the definition of insolvency | ○ | ○ | ○ | ◉ | ○ |
| d) Measures to lay down the duties of directors in companies in financial distress | ○ | ○ | ◉ | ○ | ○ |
| e) Measures to protect new financing given to companies that are being restructured | ○ | ◉ | ○ | ○ | ○ |
| f) Measures to clarify the position of shareholders of companies in insolvency or close to insolvency | ○ | ○ | ○ | ◉ | ○ |
| g) Measures to promote assistance to financially distressed debtors | ○ | ○ | ○ | ◉ | ○ |
| h) Other measures | ○ | ◉ | ○ | ○ | ○ |

**Please specify which other measures have an impact on saving viable businesses.**

The Transfer of Undertaking Directive (at least as implemented in the UK in respect of administrations) reduces the flexibility that is often required to save businesses (and, therefore, jobs).

**SPECIFIC QUESTIONS**

**2.3. If creditors are situated in a different Member State(s) than their debtors, what impact does this have on the restructuring of the business of debtors as opposed to a purely national situation?**

- a) Very significant impact
- b) Significant impact
- c) Little impact
- d) No impact at all
- e) No opinion

**Please explain your choice, including which aspects are particularly affected.**

The impact of creditors in other jurisdictions is largely of a practical nature, for instance increased costs of notifying creditors and difficulties in language. The EU Insolvency Regulation requires creditors in one member state to be treated equally with equivalent creditors in other member states but dealing with creditors in other jurisdictions may involve more work/costs for insolvency practitioners.

**2.4. When should debtors have access to a framework of restructuring measures enabling them to restructure their business/liabilities?**

- a) Only once the debtor is already insolvent
- b) Before the debtor is insolvent, but where there is a likelihood of imminent insolvency (for example because the debtor has lost a major client)
- c) At any time
- d) At another moment in time
- e) No opinion

**2.4.1. Should such restructuring measures always require, at some stage, the opening of some sort of a formal procedure in which a court (or other competent authority or body) is involved?**

- ○ a) Yes, as of the beginning of the negotiations on a restructuring plan
- ○ b) Yes, from the moment it becomes necessary to stay enforcement actions (moratorium) or obtain confirmation for the restructuring plan
- ◉ c) No, the involvement of a court should not be an absolute requirement
- ○ d) Other options
- ○ e) No opinion

**2.4.2. Should such restructuring procedures always require publicity (e.g. through an Insolvency Register)?**

- ○ a) Yes, as of the beginning of the negotiations on a restructuring plan
- ○ b) Yes, from the moment it becomes necessary to stay enforcement actions (moratorium) or obtain confirmation for the restructuring plan
- ◉ c) No, publicity should not be an absolute requirement
- ○ d) Other options
- ○ e) No opinion

**2.5. Restructuring measures in which the courts are involved to a lesser degree (e.g. only for the confirmation of a restructuring plan) or not at all (e.g. an out-of-court process) should be available to:** (choose all that apply)

- ☑ a) Microenterprises (up to 10 employees)
- ☑ b) Small and medium-sized enterprises, excluding microenterprises
- ☑ c) Large enterprises
- ☑ d) Other
- ☐ e) No opinion

**Please explain**

We have selected (d) in order to comment. There would need to be a good reason to treat enterprises differently, given the added complexity that would result, the risk of unintended consequences/arbitrage and the fact that businesses typically change in size from time to time. We are not aware of any good reason.

**2.6. Who should do the assessment of whether a debtor is viable and fit for restructuring?**

- a) The courts or external experts appointed by the courts
- b) The debtor or external experts chosen by the debtor
- c) The creditors or external experts chosen by the creditors
- d) Other persons or bodies than those listed in points a), b) or c)
- e) No one
- f) No opinion

**Please specify who**

We have selected (d) because the format did not allow us to select (a), (b) and (c) in the alternative. We believe that each of those options may be suitable depending upon the circumstances and insolvency procedure concerned. While it will typically be preferable for the debtor or creditors, or their external experts, to make the assessment without court intervention, if they are unable to do so, there should be recourse to the courts.

**2.7. Is there a need for a common definition of insolvency at EU level?**

- a) Yes
- b) No
- c) Other
- d) No opinion

**Please explain**

Please see our earlier comments regarding the need for EU harmonization generally. It is clearly important that each member state has a clear definition so that those investing in business are able to assess their rights and obligations.

If the Commission concludes that a common definition is required, it should be a definition that identifies principles (eg insolvency on a balance sheet or liquidity basis) sufficiently broadly so that those member states which already have well understood and satisfactory definitions in their regimes, with a history of interpretation of many individual cases, are not required to change their definition, with the high risk of unintended consequences that might entail.

We believe that there is a place for both balance sheet and liquidity tests.

**2.8. Should debtors in the context of restructuring measures be able to keep control over the day-to-day operations of their business (so-called 'debtor-in-possession arrangements')?**

- a) Yes, without any supervision or control
- b) Yes, but subject to supervision from a suitably qualified mediator/ supervisor/ court
- c) Yes, but subject to conditions other than supervision from a suitably qualified mediator/ supervisor/ court
- d) No, debtors should not be able to keep control over the day-to-day operations at all
- e) Other
- f) No opinion

**Please explain**

Debtors are able to restructure and remain in control in the course of their ordinary business (ie before insolvency occurs or is imminent). If the debtor is insolvent and the business is to be wound up, then it would not be appropriate for the debtor to remain in control.

Please see our general comments regarding the role of the EU in these matters. In general, where formal insolvency measures are invoked then we think that (b) or (c) above should apply if the debtor is to remain in control, although 'supervision' of the court suggests a more active role than might be required (a court might, for instance, be called upon only in certain circumstances and to determined particular matters).

**2.9. When should debtors be able to ask for a stay of individual enforcement actions?**

- a) Only in formal insolvency proceedings
- b) In formal insolvency proceedings and in preventive/pre-insolvency restructuring procedures
- c) Other
- d) No opinion

**Please explain**

**2.9.1. For how long should the enforcement of actions of individual creditors be stayed once the restructuring attempts are ongoing?**

- a) 2-3 months, without the possibility of renewal
- b) 4-6 months, without the possibility of renewal
- c) 2-3 months, with the possibility of renewal in certain circumstances
- d) 4-6 months, with the possibility of renewal in certain circumstances
- e) Any time limit set by the court subject to the fulfilment of certain conditions
- f) Other
- g) No opinion

**Please explain**

We assume that this refers only to actions where the debtor remains in possession. In that case, a relatively short period seems appropriate or creditors may be prejudiced.

**2.9.2. Should an individual creditor be allowed to ask the court to lift the stay granted to the debtor?**

- a) Yes, in all cases
- b) Yes, subject to certain conditions
- c) No
- d) Other
- e) No opinion

**Please explain**

In general, creditors should be treated equally, but there may be exceptional cases where individual creditors need protection so as not to be unfairly prejudiced.

**2.10. Should a restructuring plan adopted by the majority of creditors be binding on all creditors provided that it is confirmed by a court?**

- a) Yes, including on secured creditors
- b) Yes, but secured creditors should be exempted
- c) No
- d) Other
- e) No opinion

**Please explain**

Restructuring plans should only be binding on senior classes of creditor where that class has voted in favour.

**2.10.1. Should a 'cross-class cram down' (i.e. the confirmation of the restructuring plan supported by some classes of creditors in spite of the objections of some other classes of creditors), be possible?**

- a) Yes, in all cases
- b) Yes, but subject to certain conditions
- c) No
- d) Other
- e) No opinion

**Please specify**

Junior classes should not be able to force cram down.

**2.11. Should financing necessary for the implementation of a restructuring plan/ensuring current operations be protected if the restructuring subsequently fails and insolvency proceedings are opened?**

- a) Yes, always
- b) Yes, but only if agreed in the restructuring plan and confirmed by the court
- c) No, never
- d) Other
- e) No opinion

**2.12. Should directors of companies be incentivised to take appropriate preventive measures if companies are in distress but not yet insolvent, for example by being able to avoid related liability?**

- a) Yes
- b) No
- c) Other
- d) No opinion

**Please explain**

Directors should be deterred from carrying on business through an insolvent company. This in itself provides an incentive for directors to seek to avoid insolvency (as does common sense, as directors presumably want their business to be successful). We do not believe that directors should be relieved of their legal responsibilities by reference to the taking of preventative measures.

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

- a) Yes, for all debtors
- b) Yes, but only for SMEs
- c) Yes, but only for SMEs and individuals
- d) Yes, but only for individuals
- e) No
- f) Other actions
- g) No opinion

**Please explain**

We have selected this option in order to comment. We do not believe that this is a matter for the EU.

## 3. Second chance

The Competitiveness Council in May 2011[3] invited Member States to promote a second chance for entrepreneurs by limiting, where possible, the discharge period and enabling debt settlement for honest entrepreneurs once they are insolvent. An 'honest' failure is a case in which the business failure occurred through no obvious intentional fault of its owner or director, i.e. it was honest and above-board. This would be contrary to cases in which the bankruptcy was fraudulent, for example where the debtor transferred its assets outside the jurisdiction, made an advance payment to a single creditor, accumulated excessive private expenses, etc.

An important element to support an effective second chance regime is the 'time to discharge'. This is the time from when an entrepreneur enters into insolvency proceedings to when he/she can effectively restart an entrepreneurial activity. Currently, the discharge time varies significantly from country to country. In some countries, honest entrepreneurs in bankruptcy are automatically granted a discharge immediately once liquidation of the assets is finished. In others, bankrupted entrepreneurs have to apply for a discharge, while in some countries they cannot obtain discharge at all.

Furthermore, the procedures to release consumers from a 'debt trap' vary significantly between Member States. In some countries, there is no bankruptcy or debt settlement procedure for consumers. In others, a general insolvency regime with some changes applies to consumers.

[3] Council of the European Union, Competitiveness (Internal Market, Industry, Research and Space), Brussels, 30 and 31 May 2011. Press release available at: https://www.consilium.europa.eu/uedocs/cms_data/docs/pressdata/en/intm/122359.pdf.

**3.1. Should honest debtors (entrepreneurs and consumers) who are over-indebted be offered the chance to restructuring their debt?**

- (●) a) Yes, entrepreneurs (individuals) as well as consumers
- ( ) b) Only entrepreneurs (individuals) for debts related to their professional activity
- ( ) c) Only consumers
- ( ) d) Neither entrepreneurs (individuals) nor consumers
- ( ) e) Other options
- ( ) f) No opinion

**Please explain**

A properly controlled restructuring will generally increase the overall return to creditors in both cases. The distinctions between entrepreneurs and consumers are becoming increasingly blurred as technological and other developments allow small scale home based money making activity to flourish. See below regarding honesty.

**3.1.1. To what extent do existing differences between the laws of Member States in the area of second chance affect the functioning of the Internal Market?**

*(For example, differences affect the Internal Market when creditors or investors and debtors are located in different Member States and this has an impact on the recovery of debts, the legal certainty of transactions, the quantification of risks etc.)*

- a) To a large extent
- b) To a considerable extent
- c) To some extent
- d) Not at all
- e) No opinion

**3.2. Should over-indebted individuals have access to free or low cost debt advice?**

- a) Yes, entrepreneurs (individuals) and consumers, possibly subject to certain conditions
- b) Only entrepreneurs (individuals) for debts related to their professional activity, possibly subject to certain conditions
- c) Only consumers, possibly subject to certain conditions
- d) Neither entrepreneurs (individuals) nor consumers
- e) Other options
- f) No opinion

**Please explain what particular conditions, if any, should be attached to such access.**

We do not know what sort of conditions are envisaged here and, in any case, these sorts of matter are for individual member states. Those giving advice, whether or not for a fee, should be appropriately qualified and subject to an appropriate regulatory framework. However, care needs to be taken to ensure that they regulatory environment is not too restrictive. For instance, if those giving advice are subject to onerous financial services regime authorization, the pool of potential advisors may be too small (and the regulatory cost might need to be recovered). The regulatory position needs to be clear, with risk of inappropriate requirements for dual qualification avoided.

**3.3. Should a full discharge of debts, possibly subject to certain conditions, be offered to all over-indebted individuals provided they are 'honest' debtors?**

- a) Yes, to entrepreneurs (individuals) and consumers
- b) Only to entrepreneurs (individuals) for debts related to their professional activity
- c) Only to consumers
- d) Neither to entrepreneurs (individuals) nor to consumers
- e) Other options
- f) No opinion

**Please explain**

Discharge should apply to entrepreneurs and consumers, but the conditions may differ. See below regarding determination of honesty.

**3.3.1. Should the test of 'honesty' be made the same across all EU Member States?**

- a) Yes
- b) No
- c) No opinion

**3.3.2. What should be the maximum discharge period for honest debtors who cannot repay their debts (in other words, what should be the period after which such debtors would be completely discharged from debt, as long as they meet the obligations imposed by national laws)?**

- a) 1 year or less
- b) 3 years
- c) 5 years
- d) More than 5 years
- e) Other
- f) No opinion

**Please explain**

We think that 1 year is sufficient so long as there is opportunity for creditors to apply for suspension of discharge in relevant cases.

**3.3.3. . In the case of debtors that are insolvent, should a full discharge be conditional on the repayment of a certain amount of debt?**

- a) Yes
- b) No
- c) Other options
- d) No opinion

**3.3.4. Which special types of debt should be excluded from discharge?** (choose all that apply)

- [ ] a) Tort claims
- [ ] b) Fines
- [x] c) Child support
- [ ] d) Tax and other public liabilities
- [x] e) Other types of debt
- [ ] f) No opinion

**Please specify**

The types of debt should be narrowly defined or the concept of a second chance would be diluted. But bankruptcy should not be a lifestyle option and there is a balance between giving people a second chance and promoting inappropriate or even reckless borrowing behaviour at the expense of creditors who rely upon honest behaviour in repayment of their debts.

**3.4. If it is decided that the discharge of debts should be offered to all individuals, whether entrepreneurs or consumers, should the conditions for the discharge be the same?**

- (•) a) Yes
- ( ) b) No, the conditions applicable to entrepreneurs should be stricter than those applicable to consumers
- ( ) c) No, the conditions applicable to consumers should be stricter than those applicable to entrepreneurs
- ( ) d) Other options
- ( ) e) No opinion

**3.4.1. Please explain**

It is preferable to keep the regime as simple as possible so that the position is clear for all involved. If 'entrepreneurs' are to be treated differently from 'consumers' there is a risk that one individual could be in a better position than another in respect of debt incurred in relation to non-business matters merely because he or she is defined as an 'entrepreneur', which would be relatively unfair to consumers.

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

The efficient and effective recovery of debts depends on many factors. The recovery rates of debts may depend on:

- the effectiveness of insolvency proceedings;
- their length;
- the specialisation of the people dealing with them;
- the qualification of the directors of distressed companies.

The recovery rate of debts also has an impact on high levels of non-performing loans in the EU.

The laws of Member States differ significantly on the priority of claims in insolvency. This has an impact on how insolvency proceedings are run and how debts are recovered. Laws also differ on possibilities for avoiding contracts detrimental to companies and creditors. Differences concern conditions under which a detrimental act can be avoided (avoidance actions) and the period within which such acts can be challenged.

Also, the laws of Member States have different rules on insolvency practitioners themselves, namely the qualifications and eligibility for their appointment and also their licensing, regulation, supervision, professional ethics and conduct. The questions related to insolvency practitioners concern any mediators or supervisors engaged in the insolvency process. Moreover, in most Member States, insolvency proceedings are administered by a judicial authority, often through commercial courts, courts of general jurisdiction or through specialised insolvency courts. Sometimes judges have specialised knowledge and responsibility for insolvency matters, while in other cases insolvency matters are just one of a number of wider judicial responsibilities of the courts.

There is currently no rule at EU level which ensures that directors who have been disqualified in one Member State, e.g. because of fraudulent behaviour, are prevented from setting up a new company or from being appointed as director of a company in another Member State. This means that disqualified directors can easily move from one Member State to another and manage companies in the EU even if they were not allowed to, at least for a certain period of time, in the Member State that disqualified them. The European Commission supports cross-country access to information about whether directors have been disqualified. The Commission will establish a decentralised system to interconnect insolvency registers. Under this system, Member States are invited, in accordance with Article 24(3) of Regulation (EU) 848/2015, to include in their national insolvency registers documents or additional information such as insolvency-related disqualifications of directors.

**GENERAL QUESTIONS**

**4.1. To what extent do existing differences between the laws of the Member States in the areas mentioned below affect the functioning of the Internal Market?**

*(For example, differences affect the Internal Market when creditors or investors and debtors are located in different Member States and this has an impact on the recovery of debts, the legal certainty of transactions, the quantification of risks etc.)*

| | To a large extent | To a considerable extent | To some extent | Not at all | No opinion |
|---|---|---|---|---|---|
| a) Minimum standards on the ranking of claims in formal insolvency proceedings | ○ | ○ | ◉ | ○ | ○ |
| b) Minimum standards on avoidance actions | ○ | ○ | ◉ | ○ | ○ |
| c) Minimum standards applicable to insolvency practitioners/mediators/supervisors | ○ | ○ | ◉ | ○ | ○ |
| d) Measures providing for a specialisation of courts or judges | ○ | ○ | ○ | ◉ | ○ |
| e) Measures to shorten the length of insolvency proceedings | ○ | ○ | ○ | ◉ | ○ |
| f) Measures to prevent disqualified directors from starting new companies in another Member State | ○ | ○ | ○ | ◉ | ○ |
| g) Other measures | ○ | ○ | ○ | ○ | ◉ |

**Please explain**

Please see our response to Q1.2. These are all issues that need to be considered by member states, but an effective insolvency regime depends upon all the different elements working together effectively. If an element is working effectively, such as the court system, then there will be no adverse impact on the functioning of the EU market even if the result is not achieved in the same way as in other member states.

**4.2. Which measures would contribute to increasing the recovery rates of debts?** (choose all that apply)

- [ ] a) Minimum standards on the ranking of claims in formal insolvency proceedings
- [ ] b) Minimum standards on avoidance actions
- [x] c) Minimum standards applicable to insolvency practitioners/mediators/supervisors
- [ ] d) Measures providing for a specialisation of courts or judges
- [ ] e) Measures to shorten the length of insolvency proceedings
- [ ] f) Measures to prevent disqualified directors from starting new companies in another Member State
- [x] g) Other measures
- [ ] h) No opinion

**Please explain**

We have highlighted point (c) as being the most significant, but a robust regime on most of the other issues is also important. We do not, however, believe that shortening the length of insolvency proceedings should be an aim in its own right as the priority should be to ensure that recoverable assets are indeed recovered.

**SPECIFIC QUESTIONS**

**4.3. Which claims should have priority in insolvency proceedings (i.e. be satisfied first from the proceeds of the insolvent estate)?** (choose all that apply)

- [x] a) Secured creditors should be satisfied in principle before all other creditors
- [ ] b) Secured creditors should be satisfied before unsecured creditors but not before privileged creditors such as employees and/or tax and social security authorities
- [ ] c) Tort claims should have a higher priority than other unsecured claims
- [ ] d) Other ranking of priorities
- [ ] e) No opinion

**Please explain**

If secured creditors do not have priority, the security will be weakened and willingness to provide finance may be diminished. This applies to all the various forms of security, including, in the UK, floating charges (with allowance made for some preferential claims). Costs of insolvency also need to be paid first.

**4.4. What minimum standards should be harmonised for 'avoidance actions'?** (choose all that apply)

- [ ] a) Rules on the types of transactions which could be avoided
- [ ] b) Rules on 'suspect periods' (periods of time before insolvency when a transaction is presumed to be detrimental to creditors)
- [x] c) Other rules
- [ ] d) No opinion

**Please explain**

We do not believe that the EU should attempt to harmonise standards on 'avoidance' – please see earlier comments on the role of the EU.

**4.5. In what areas would minimum standards for insolvency practitioners help to increase the efficiency and effectiveness of insolvency proceedings?** (choose all that apply)

- [x] a) Licensing and registration requirements
- [ ] b) Personal liability
- [ ] c) Subscribing to a professional liability insurance scheme
- [x] d) Qualifications and training
- [x] e) Code of ethics
- [x] f) Other
- [ ] g) No standards should be harmonised
- [ ] h) No opinion

**Please specify**

ICAEW is a licensing body with high standards of qualification and training and a robust code of ethics. We believe that our members have contributed greatly to the effectiveness of insolvency processes with which they have been involved.

**4.6. Which additional minimum standards, if any, should be imposed on insolvency practitioners specifically dealing with cross-border cases?** (choose all that apply)

- [ ] a) Relevant foreign language knowledge
- [x] b) Sufficient human and financial resources in the insolvency practitioner's office
- [ ] c) Pre-defined period of experience
- [x] d) Others
- [ ] e) No additional standards are needed compared with those relevant for domestic insolvency cases
- [ ] f) No opinion

**Please specify**

Practitioners will typically engage local experts when involved in cross border cases and will select those with appropriate language skills and experience. They do, however, have to have requisite skill in identifying an working with such experts and this may be easier where those experts are subject to the standards highlighted in our answer to Q4.5.

**4.7. What are the causes for the excessive length of insolvency proceedings?** (choose all that apply)

- [ ] a) Judicial activities concerning the supervision or administration of insolvency proceedings
- [ ] b) Delays in the liquidation of the debtor's assets
- [x] c) The time taken to obtain final decisions on cases concerning the rights and duties of the debtor (e.g. claims, debts, disputed property in goods)
- [x] d) A lack of promptness in exercising creditors' rights
- [ ] e) Lack of electronic means of communication between the creditors and relevant national authorities, such as for the purposes of filing of claims, distance voting etc.
- [ ] f) Other
- [ ] g) No opinion

**Please explain**

Judicial supervision activities in the UK are not generally excessively long, but we are aware of delays in other jurisdictions. It can take a long to time to liquidate assets where there is a dispute (ie under (c) above).

**4.8. Would a target maximum duration of insolvency proceedings — either at first instance or including appeals — be appropriate?**

- ○ a) Yes
- ○ b) Yes, but only for SMEs
- ◉ c) No
- ○ d) Other possibilities
- ○ e) No opinion

**4.9. What incentives could be put in place to reduce the length of insolvency proceedings?** (please explain)

We do not believe that incentives are required if an appropriate framework exists. There is a risk that setting time limits will result in unnecessary extra work and cost, because the reasons for delay are often outside the control of those involved and extensions may need to be obtained (more often the shorter the time limit).

**4.10. When disqualification orders for directors are issued in one Member State (i.e. the 'home State'), they should:**

- ☑ a) be made available for information purposes via the interconnected insolvency registers so that other Member States are informed
- ☐ b) automatically prevent disqualified directors from managing companies in other Member States
- ☑ c) not automatically prevent disqualified directors from managing companies in other Member States, but make them subject to intermediary steps (e.g. a court order)
- ☐ d) Other options
- ☐ e) No opinion

**Please explain**

It is important that those involved have the relevant information to make informed decisions. However, the reasons for disqualification may vary from one member state to another (for instance different criminal laws might apply), as may the interpretation and application of the rules by courts and tribunals. Disqualification should not therefore be automatic.

**4.11. Directors disqualified in one Member State (home State) should be prevented from managing companies in other Member States (host States):** (choose all that apply)

- [ ] a) Always
- [ ] b) Only for the duration applicable to equivalent disqualification orders in the host State
- [ ] c) Only in the same or similar sector of activity
- [ ] d) Never
- [x] e) Other options
- [ ] f) No opinion

**Please explain**

See our response to Q4.10 above.

**4.12. Which measures would contribute to reducing the problem of non-performing loans?** (choose all that apply)

- [ ] a) Measures to improve the effectiveness of insolvency proceedings
- [ ] b) Measures enabling the rescue of viable businesses
- [ ] c) Measures to provide user-friendly information about national insolvency frameworks
- [ ] d) Measures to ensure a discharge of debts of entrepreneurs (individuals)
- [ ] e) Measures to ensure a discharge of debts of consumers
- [ ] f) Other measures related to insolvency
- [x] g) Measures unrelated to insolvency (e.g. enforcement of contracts)
- [ ] h) No opinion

**Please explain**

What measures are relevant will depend upon the circumstances. For instance, if rescue is not viable, insolvency measures designed to recover the maximum amount of the loan in an efficient way will be relatively important.

## 5. Additional comments

**Are there any additional comments you wish to make on the subject covered by this consultation?**

Please see our general comments on the role of the EU in answer to Q1.2.

We do not believe that the test of 'honesty' should be made the same across the EU, but as question 3.3.1 did not give room for explanation we comment further here. To the extent that the term is intended to refer to the state of mind of a person (as we think it ordinarily would), this would be a matter for courts to determine on the basis of all the circumstances, not something for the EU to define. If, however, protections for 'honest' entrepreneurs are to be subject to objective tests, such as incurring debts when bankrupt or previous history of bankruptcy, then those issues would need to be considered separately and seem to be matters of relative detail where harmonization would be over intrusive.

**You can also send a separate written contribution by uploading your document here:**

## Contact

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