PROPOSAL FOR A DIRECTIVE OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL HARMONISING CERTAIN ASPECTS OF INSOLVENCY LAW - INTRODUCTORY ASPECTS

Vasile NEMEȘ[*]

Gabriela FIERBINȚEANU[**]

Abstract

Insolvency is an area inextricably linked to the evolution of investment, capital markets and the single market, the convergence of insolvency regimes at Member State level being a major concern of the European legislator.

However, given that existing EU legislation only covers pre-insolvency and debt relief measures as well as the rules on applicable law in cross-border insolvency cases, disparities between national rules remain in the substantive regulation of this area, which creates difficulties for stakeholders and discourages cross-border investment.

The new legislative proposal, which opts for targeted intervention, aims to ensure economic benefits for investors, creditors, businesses (including micro-enterprises) by reducing legal uncertainty in the case of insolvent debtors. Clearly action at European level is more appropriate to ensure convergence of specific elements of Member States' insolvency rules. EU level measures would ensure a level playing field, facilitating cross-border investment and contributing to the achievement of a robust Capital Markets Union.

Without wishing to give an exhaustive presentation of the proposal, we will try to focus on some of the novelties, in particular pre-pack procedures, avoidance actions and the simplified procedure for the winding-up of micro-enterprises, while also referring to the provisions of the relevant national rules (Law no. 85 of 25 June 2014 on pre insolvency and insolvency proceedings).

Keywords: *convergence of insolvency rules, pre-pack proceedings, avoidance actions, liquidation of micro-enterprises, role of the insolvency practitioner.*

1. Introduction

The Proposal for a Directive of the European Parliament and of the Council on the harmonisation of certain aspects of insolvency law, launched by the European Commission on 7 December 2022 (hereinafter „the Directive") is, as stated in the Explanatory Memorandum of this legislative initiative, part of the European Commission's line of action to promote the Capital Markets Union[1], a project that is essential for further financial and economic integration in the EU. Although the Restructuring and Insolvency Directive (EU) 2019/1023 was also the fruit of a strategy to accelerate reforms dedicated to the Capital Markets Union, it appears that, according to ECB[2] or IMF analyses, there was an additional need to address the deficiencies and divergences in insolvency rules beyond the framework of the first Directive, this time aiming at targeted harmonisation of certain aspects of substantive insolvency law.

As a first general comment, we note that, in estimating the chances of success of such an exercise to reduce the differences between national procedures, the European legislator reasonably proposes minimum harmonisation requirements selecting only those areas of substantive law that can support an intervention accepted by the Member States. The proposal for a Directive aims to reduce differences between insolvency

[*] Associate Professor, PhD, Faculty of Law, „Nicolae Titulescu" University of Bucharest (e-mail: nemes@nemes-asociatii.ro).

[**] Lecturer, PhD, Faculty of Law, „Nicolae Titulescu" University of Bucharest (e-mail : gabriela.fierbinteanu@gmail.com).

[1] Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of Regions, *A Capital Markets Union for Citizens and Business - A New Action Plan*, COM(2020) 590 final, *eur-lex.europa.eu/legal-content/EN/TXT/HTML/?uri=CELEX:52020DC0590*.

[2] ECB, *Financial integration in Europe*, May 2018, *https://www.ecb.europa.eu/pub/pdf/fie/ecb.financialintegrationineurope201805.en.pdf*, and *Financial Integration and Structure in the Euro Area*, April 2022, *https://www.ecb.europa.eu/pub/pdf/fie/ecb.fie202204~4c4f5f572f.en.pdf*.

laws and thus address the problem of less effective insolvency rules in certain Member States, increase the predictability of insolvency proceedings in general and reduce obstacles to the free movement of capital. By harmonising specific aspects of insolvency law, the proposal aims in particular at facilitating cross-border investment by reducing costs for investors. The Directive complements the relevant Union framework, namely Directive (EU) 2019/1023 of the European Parliament and of the Council[3] and Regulation (EU) 2015/848 of the European Parliament and of the Council[4], by addressing issues not regulated by them.

2. Structure of the legislative proposal and first reactions

The proposed Directive is structured in nine titles: Title I - General provisions - under this title the scope and definitions are included; Title II - Avoidance actions - both general and specific conditions for bringing actions for annulment and their consequences are set out; Title III - Tracing of assets belonging to the debtor's estate - the Title includes provisions concerning access to bank information by certain designated courts, access to the register of beneficial owners and national asset registers by insolvency practitioners; Title IV - *Pre-pack* proceedings - includes general provisions, the preparatory stage, the liquidation stage; Title V - Duty of directors to request the opening of insolvency proceedings and civil liability; Title VI - Winding-up proceedings for micro-enterprises - this title contains general rules, opening of simplified winding-up proceedings, list of claims and determination of the mass of assets subject to insolvency, valuation of assets and distribution of proceeds, remittance of debts of entrepreneurs in simplified winding-up proceedings; Title VII - Creditors' committee - rules are laid down for the establishment of the creditors' committee, its members and its functioning; Title VIII - Measures to increase transparency in national insolvency laws; Title IX - Final provisions. The key dimensions of the proposal, also derived from art. 1 of the proposal (Subject matter and scope) are: (i) recovery of assets from the liquidated estate; (ii) efficiency of proceedings; and (iii) predictable and fair distribution of the value recovered among creditors.

It should be noted that immediately after the Proposal appeared, EESC expressed doubts as to whether the proposal would be a significant step towards closing the relevant gaps for the improvement of the European capital market Union, given that the Directive fails to provide a harmonised definition of the grounds for insolvency and the ranking of claims, both of which are essential for achieving greater efficiency and limiting the fragmentation of national insolvency rules[5]. Recently, the Eurogroup Inclusive Statement on the Future of the Capital Markets Union called on the European Commission to assess the need for further measures to facilitate greater convergence on specific features of insolvency frameworks that could discourage cross-border capital markets/investment, in particular the ranking of claims and triggers of insolvency or rules on financial collateral and settlement[6].

3. Introductory considerations about some of the policy options

We present below some considerations on some of the preferred policy options of the proposal, following some key elements of their architecture. It should be noted that the Directive is currently under consideration by the preparatory bodies of the Council of the EU.

3.1. Title II - Avoidance actions

Title II on actions for voidness provides for minimum harmonisation rules designed to protect the estate subject to insolvency proceedings against unlawful disposal of assets prior to the opening of insolvency proceedings. The objective is to ensure that the national rules of Member States on insolvency proceedings provide a minimum standard of protection as regards the voidness, voidability or unenforceability of legal acts

[3] Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency) (OJ L 172/26.06.2019.

[4] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (OJ L 141/05.06.2015.

[5] Opinion of the European Economic and Social Committee on the „Proposal for a directive of the European Parliament and of the Council harmonising certain aspects of insolvency law", OJ L C 184/34/25.05.2023), Opinion of the European Economic and Social Committee on the „Proposal for a directive of the European Parliament and of the Council harmonising certain aspects of insolvency law" (COM(2022)702 final – 2022/0408 (COD)) (*europa.eu*).

[6] Statement of the Eurogroup in inclusive format on the future of Capital Markets Union – Consilium (*europa.eu*).

detrimental to the estate. At the same time, Member States may introduce or maintain rules ensuring a higher level of protection for creditors, for example by providing for more grounds for avoidance. In the context of the proposed framing of art. 6(1) supara. 1, it is important to determine objectively the limits of the suspect period, as the proposed rule is perfectible („*the submission of a request for the opening of insolvency proceedings, provided that the debtor has been unable to pay his debts as they fall due*"). In national law, according to art. 5 point 29 of Law no. 85/2014 on insolvency proceedings and insolvency proceedings, both manifest and presumed insolvency are taken into account, but art. 66 of Law no. 85/2014 operates separately both with the debtor's obligation to submit an application for the opening of proceedings if the debtor is in a state of insolvency and with the debtor's right to submit an application for the opening of proceedings if the debtor is in a state of imminent insolvency. Art. 6(1)(2) of the Directive retains the criterion of admissibility of the first application filed, which, by reference to art. 66(7) of Law no. 85/2014[7] (debtor's application and several creditors' applications) and art. 70(3) of the same national rule (several creditors' claims) generates a process of reflection. With regard to the derogations proposed by art. 6(3) of the Directive, the phrase *fair consideration* present in point (a) would be a potential candidate to increase the level of clarity, *fairness for the benefit of the mass of assets subject to insolvency*, allowing a wide range of interpretation. With reference to the general preconditions for actions for annulment, the sentence of art. 4 of the Directive indicates the possibility of declaring void legal acts „*completed*" before the opening of the procedure, *verbum regens* implying the conclusion/perfection, therefore an action. However, the definition proposed in art. 2(f) for legal act refers to *any human conduct, including an omission, which produces a legal effect*. Looking at the explanations provided by the recitals, we note in recital 6 some reasoning designed to give consistency to the option of including omissions within the scope of legal acts, based on the idea that *„it makes no significant difference whether creditors suffer damage as a result of an action or as a result of the passivity of the party concerned. For example, it makes no difference whether a debtor actively waives a claim against his debtor or whether he remains passive and accepts the statute of limitations. Other examples of omissions that may be subject to actions for annulment include failure to challenge a disadvantageous court judgment or other decisions of courts or public authorities or failure to register an intellectual property right*". We limit ourselves to observing, in the light of the above references, that a legal act cannot exist in the absence of a manifestation of will, being impossible to conclude it by omission. Human acts (whether committed or omitted), committed without the intention of producing legal effects although they produce effects by the will of the law, fall within the category of legal facts *stricto sensu* which constitute the source of legal relationships under private law. Last but not least, in order to draw attention to the vulnerability of art. 16 (former art. 13) of Regulation (EC) 1346/2000 on insolvency proceedings, we recall in the discussion of actions for annulment, the case law of the CJEU which upholds the protection afforded to the expectations of third parties concluding a contract with the insolvent debtor. We exemplify these concerns by two landmark judgments, namely the judgment in Vinyls (C-54/16[8]) which held that *„art. 13 of Regulation no. 1346/2000 may be validly relied upon where the parties to a contract, who have their head offices in a single Member State on whose territory all the other elements relevant to the situation in question are located, have designated the law of another Member State as the law applicable to that contract, provided that those parties did not choose that law for abusive or fraudulent ends, that being a matter for the referring court to determine*" and the judgment in Frerichs[9] (C-73/20) in which the Court concluded that *„Art. 13 of Council Regulation (EC) no. 1346/2000 of 29 May 2000 on insolvency proceedings and art. 12(1)(b) of Regulation (EC) no. 593/2008 of the European Parliament and of the Council of 17 June 2008 on the law applicable to contractual obligations (Rome I) must be interpreted as meaning that the law applicable to the contract under the latter regulation also governs the payment made by a third party in performance of a contracting party's contractual payment obligation where, in insolvency proceedings, that payment is challenged as an act detrimental to all the creditors".* Another novelty compared to national law in this area is that actions for annulment do not only concern acts of the debtor to the detriment of creditors, but also of the co-contracting party or a third party.

[7] Law no. 85/2014 on pre insolvency and insolvency proceedings, published in the Official Gazette of Romania no. 466/25.06.2014.
[8] Case *Vinyls Italia SpA v. Mediterranea di Navigazione SpA*, C-54/16, ECLI:EU:C:2017:433.
[9] Case *ZM v. E.A.Frerichs*, C-73/20, judgment of the Court (First Chamber) of 22.04.2021, ECLI:EU:C:2021:315.

3.2. Title III - Tracing assets belonging to the insolvency estate

The proposed rules aim to give insolvency practitioners access to various registers containing relevant information on assets belonging or supposed to belong to the insolvency estate. Some national electronic registers are public or accessible through single interconnection platforms set up by the EU, such as the Insolvency Registers Interconnection (IRI) system. The provisions of the Directive extend the scope of registers accessible to insolvency practitioners to registers originally established under the EU anti-money laundering framework (central national registers of bank accounts or trust information in Member States' beneficial ownership registers).Title III also obliges Member States to provide foreign insolvency practitioners with direct and rapid access to the registers listed in the Annex (as long as they are already available in the Member State). We also note the developments proposed in recital 16 concerning the organisation of access to these registers *„In order to respect the right to the protection of personal data and the right to privacy, direct and immediate access to bank account registries should be granted only to courts with jurisdiction in insolvency proceedings that are designated by the Member States for that purpose. Insolvency practitioners should therefore be allowed to access information held in the bank account registries only indirectly by requesting the designated courts in their Member State to access and run the searches".* We consider that the way in which access to these registers will be materialised, without challenging the proposed circulation circuit, should not affect the speed of the procedure. In this respect, the provisions of art. 15 of the Directive, which regulates the conditions for accessing and consulting information and provides for a case-by-case analysis, must be reconciled with circumstances such as those set out in art. 14(4), „access and consultation shall be deemed to be direct and immediate", which refers only to the hit back provided by the automated register of bank accounts accessed, without imposing deadlines for making the request. In the context of the discussions on access of insolvency practitioners to registers in other Member States, we also recall the provisions of art. 33 of Regulation (EU) 2015/848 (recast) which stipulates that *„Any Member State may refuse to recognise insolvency proceedings opened in another Member State or to enforce a judgment handed down in the context of such proceedings where the effects of such recognition or enforcement would be manifestly contrary to that State's public policy, in particular its fundamental principles or the constitutional rights and liberties of the individual".* This provision may imply that „the power of pursuit and recovery of assets" enjoyed by the insolvency practitioner under the *lex concursus* is diminished when it conflicts with the public policy of the requested State. Therefore, if the pursuit and recovery measures were not known to the State in which the assets are located because they are incompatible with its public policy, they would not be enforced. We also mention the imperative of aligning access to beneficial ownership registers with the safeguards listed in the CJEU judgment of 22 November 2022 in Joined Cases C-37/20 and C-601/20[10] and of monitoring, in parallel with the analysis of the text of the proposal, the discussions taking place at UNCITRAL level, Working Group V (Insolvency) on possible developments in the field of asset tracing.

3.3. Title IV - Pre-pack proceedings

Title IV on pre-pack procedures aims to ensure that these procedures, which are generally considered to be effective in recovering value for creditors, are available in a structured manner in the insolvency regimes of all Member States. *Pre-pack* procedures consist of a preparation phase and a liquidation phase. The sale of all or part of the debtor's business is prepared and negotiated prior to the opening of insolvency proceedings. The debtor in financial difficulty, under the supervision of a person monitoring the process („*monitor*"), identifies potential buyers by preparing the sale. In order to ensure that the sale is made at the best market price, the Member States must either implement high standards of competitiveness, transparency and fairness in the *pre-pack* preparation phase or provide that the competent court will conduct a public auction after the start of the liquidation phase. This allows the sale to be executed and the proceeds collected shortly after the opening of formal insolvency proceedings for the winding-up of a company. This proposal includes a number of safeguards to ensure that potential buyers are contacted and that the best possible market value is obtained, such safeguards being formulated in such a way as to give Member States a choice between ensuring the competitiveness, transparency and fairness of the sale process in the (usually confidential) „preparation phase" and holding a prompt public auction after the opening of the formal procedure in the „liquidation phase". The major advantage of pre-pack proceedings is that a recovery plan can be drawn up in advance and implemented

[10] Judgment from 22/11/2022 - *Luxembourg Business Registers*, Case C-37/20 (Joined Cases C-37/20, C-601/20) ECLI:EU:C:2022:912.

at the opening of proceedings in standard proceedings, with the insolvency practitioner's efforts to save the business starting after a series of formalities that can lead to missed opportunities. The sale of the business allows the company to operate, maintaining its good reputation even if it is practically preparing for insolvency proceedings (according to art. 23 of the Directive, the preparation stage occurs when the debtor is in a situation of likelihood of insolvency or is insolvent under national law). These systems, even if not regulated at the level of all Member States, are known in practice, being even assumed at the level of CJEU judgments (C-126/16[11]). We note in the context of the case in question the reasoning of the Advocate General, para. 57 *et seq.*, which states that *„it may be considered that a transfer takes place as part of a procedure the aim of which is the continuation of the undertaking where that procedure is designed or applied specifically in order to preserve the operational character of the undertaking (or of its viable units) in such a way as to make it possible to retain the value which stems from the uninterrupted continuation of its operations".* It can be assumed that the role of *„monitor"* would, at national level, as indicated in art. 20(1)(2) of the Directive, fall to insolvency practitioners *[Monitors referred to in art. 22 may be considered to be insolvency practitioners as defined in art. 2(5) of Regulation (EU) 2015/848*]. The reference to the test of the best interest of creditors may give rise to some reflections given that, according to art. 5 para. (1) point 71 of Law no. 85/2014, such a test is aimed at a comparative analysis of the degree of indebtedness of the budgetary claim by reference to an average diligent creditor, in the context of insolvency prevention or reorganisation proceedings, compared to bankruptcy proceedings or, in the context of the Directive, the reference factor seems ambiguous (liquidation v. continued activity). Another potential problem is the proposed suspension of individual enforcement actions during the preparation phase, or, as preparation is intended to be confidential (footnote 13 of the Directive's Explanatory Memorandum indicating that, „in pre-pack proceedings, the debtor's business or part thereof is sold as a going concern under a contract that is negotiated confidentially prior to the commencement of an insolvency proceeding under the supervision of a monitor appointed by a court and followed by a brief insolvency proceeding, in which the pre-negotiated sale is formally authorised and executed"), it is difficult to anticipate how a stay of individual enforcement actions could be implemented without the intervention of a court order, and it is difficult to see how it could be negotiated with all creditors. The argument in favor of such a decision is also to be found in the final sentence of art. 23, which states that „the monitor shall be heard prior to the decision on the stay of individual enforcement actions". As a general preliminary remark, we note some deviations from the objective of ensuring the protection of creditors' interests, which is specific to insolvency proceedings.

3.4. Title VI Winding - up of insolvent microenterprises

Title VI contains rules on simplified winding-up procedures for micro-enterprises, an intervention motivated by the inadequacy of national frameworks. Micro-enterprises rarely file applications to open standard insolvency proceedings and, when they do, it is often too late to preserve their value. In many Member States standard insolvency proceedings are not available to this type of business or the opening of such proceedings is rejected. This is the case if there are no assets in the insolvency estate or if the value of the assets does not cover the administrative costs of the proceedings. The objective of the proposed Directive is therefore to ensure that micro-enterprises, even those without assets, are liquidated through a rapid and cost-effective procedure. Although the need to simplify the procedure for micro-enterprises is obvious, its implementation could be problematic from a practical point of view. For most Member States, it is a completely new procedure, which requires re-engineering the architecture at national level. In addition, responsibilities previously exercised by the insolvency practitioner will be transferred to the court and the debtor. As the insolvency practitioner has an important role in the tracing of assets and the initiation of actions for annulment, his removal could lead to a decrease in the value of recoverable assets (creditors would have to initiate these actions themselves, but often do not have access to the relevant information and documents necessary for these claims). In addition, the tradition of the domestic insolvency mechanism, also confirmed by consultations with stakeholders in insolvency proceedings in the context of the proposed Directive, is for the proceedings to be managed by a liquidator, appointed in all cases, rather than on a case-by-case basis .It is also necessary to note, by reference to national law, the provisions of art. 47(c) of the Directive, which states that the competent authority may convert the simplified winding-up proceedings into standard insolvency proceedings if it would not be possible to conduct the cancellation proceedings in the simplified winding-up proceedings because of the size of the claims subject

[11] Case C-126/16, *Federatie Nederlandse Vakvereniging and Others v. Smallsteps BV*, ECLI:EU:C:2017:241.

to the cancellation proceedings in relation to the value of the assets subject to the insolvency proceedings and because of the anticipated duration of the cancellation proceedings, and also the option of the European legislator to allow the competent authority to decide to continue the simplified winding-up proceedings only in respect of uncontested claims [art. 46(5) of the Directive]. Another sensitive element is the way in which the definition of micro-enterprise is arranged, as the concept proposed in art. 2(j) is inappropriately based on Commission Recommendation 2003/361/EC of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises[12].

4. Conclusions

Increasing the efficiency of insolvency proceedings will contribute to a reduction in the length of insolvency proceedings and higher recovery rates for creditors and investors. Enhanced predictability of the insolvency regime would also encourage greater investments. The convergence of insolvency rules should, on the other hand, not compromise the fair treatment of debtors, creditors and other stakeholders in companies under insolvency procedures. Regardless of the final form of the text as it will emerge from the co-decision process, there can be no doubt that such action at EU level is well placed to substantially reduce the fragmentation of national regimes, and the Directive has clear potential to achieve this objective.

References

- Communication from the Commission to the European Parliament, the Council, the European Economic and Social Committee and the Committee of Regions, *A Capital Markets Union for Citizens and Business - A New Action Plan*, COM(2020) 590 final;
- ECB, „Financial integration in Europe", May 2018, „Financial Integration and Structure in the Euro Area", April 2022;
- Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 (Directive on restructuring and insolvency);
- Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (OJ L 141/05.06.2015);
- Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises;
- Opinion of the European Economic and Social Committee on the 'Proposal for a directive of the European Parliament and of the Council harmonising certain aspects of insolvency law, OJ L C 184/34/25.05.2023;
- Statement of the Eurogroup in inclusive format on the future of Capital Markets Union - Consilium (*europa.eu*);
- Vinyls Italia SpA v. Mediterranea di Navigazione SpA, C-54/16, ECLI:EU:C:2017:433;
- *ZM v. E.A.Frerichs*, C-73/20, judgment of the Court (First Chamber) of 22 April 2021, ECLI:EU:C:2021:315;
- Judgment from 22/11/2022 - *Luxembourg Business Registers*, Case C-37/20 (Joined Cases C-37/20, C-601/20) ECLI:EU:C:2022:912;
- Law no. 85/2014 on preinsolvency and insolvency proceedings, published in the Official Gazette of Romania no. 466/25.06.2014.

[12] Commission Recommendation of 6 May 2003 concerning the definition of micro, small and medium-sized enterprises, OJ L 124/20.05.2003, EUR-Lex - 32003H0361 - EN - EUR-Lex (europa.eu).