Comments to the new EU regulation on insolvency proceedings

Pre-insolvency proceedings under the EU regulation on insolvency proceedings: the Spanish case

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1. Art. 1(1)(c) of the Regulation. Appraisal

Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast, hereinafter the regulation or ERIP *bis*) includes within its scope **"pre-insolvency" proceedings**, defined as "*public collective proceedings, including interim proceedings, which are based on laws relating to insolvency and in which, for the purpose of rescue, adjustment of debt, reorganisation or liquidation, […](c) a temporary stay of individual enforcement proceedings is granted by a court or by operation of law, in order to allow for negotiations between the debtor and its creditors, provided that the proceedings in which the stay is granted provide for suitable measures to protect the general body of creditors, and, where no agreement is reached, are preliminary to one of the proceedings referred to in point (a) or (b)*". [Points (a) and (b) refer to proceedings where (a) a debtor is totally or partially divested of its assets and an insolvency practitioner is appointed; (b) the assets and affairs of a debtor are subject to control or supervision by a court].

The inclusion of pre-insolvency proceedings within the above regulatory scope is a mistake that reveals the EU legislator's ignorance as to how these proceedings work and of how their practical application is unrelated to the COMI/main proceedings structure underpinning ERIP *bis*. To begin with, any talk about COMI and the "opening" of insolvency proceedings in terms of art. 3 is absurd in the context of 'pure negotiatory' proceedings, just as it is inappropriate for such "proceedings" to be vested with judicial powers and jurisdiction over matters governed by the *lex forum concursus*, as are those provided in arts. 6 and 7 ERIP *bis*.

2. Spanish pre-insolvency proceedings

According to annex A of ERIP *bis*, refinancing arrangement homologation proceedings (*procedimiento de homologación de acuerdos de refinanciación*, 4th additional provision of the Spanish Insolvency Act [abbrev. LCon]), mediated settlement agreement proceedings ("*procedimiento de acuerdos extrajudiciales de pagos*", arts. 231 *et seq.* LCon), "*procedimientos de negociación pública para la consecución de acuerdos de refinanciación colectivos*", homologated (i.e., court-sanctioned) refinancing agreements (repeated in the regulation) and early composition with creditors ("*propuesta anticipada de convenio*", arts. 104 *et seq.* LCon). Strictly speaking, however, not all those listed are insolvency proceedings within the meaning either of ERIP *bis* or of LCon, or even "proceedings" in the proper sense of the term.

Indeed, the "*procedimientos de negociación pública para la consecución de acuerdos de refinanciación colectivos*" almost certainly refer to the "proceedings" to achieve a plural arrangement regulated under art. 71 *bis*(1) LCon. But this collective arrangement can hardly constitute insolvency proceedings within the meaning of art. 1(c) ERIP *bis*, as notwithstanding the "notification" to which art. 5 *bis*(1) LCon refers to, there is no court intervention, notwithstanding the staying effect to which art. 5 *bis*(4) LCon refers to, neither can the arrangement be crammed down on non-assenting creditors, and, if approved, such

arrangement is not concluded as collective proceedings. In fact, there will not be such a thing as "proceedings" because there is no procedural scheme allowing for the obtainment therein of plural votes, which must have been obtained in advanced. On the other hand, an early composition with creditors does not constitute insolvency proceedings, but rather is one of the methods of arriving at a composition within ordinary insolvency proceedings (the "concurso"), and has no force separate from that of the insolvency proceedings of which they form part, without prejudice to the fact that notice of its submission may have a staying effect if a stay has not already been applied for prior to the opening of the insolvency proceedings.

As things stand, proceedings opened with the notification to the judge of the commencement of negotiations to conclude a refinancing arrangement, to obtain consent to an early composition with creditors or to reach a mediated settlement agreement, are deemed to be subject to ERIP *bis*. That is to say, the regulation refers to art. 5 *bis* LCon. And this connects with art. 1(1)(c) ERIP *bis* insofar as this provision includes those proceedings where, by the operation of the law (i.e., without requiring a court decision), enforcements are stayed in order to facilitate negotiations between the debtor and its creditors. The problem, actually, is that the "proceedings" under art. 5 *bis*(4) LCon are not framed as insolvency proceedings, even though it could be said that they do give rise to a state of *concursus* (gathering creditors together insofar as deprived of the possibility of bringing individual enforcement actions).[1]

3. Irrelevance of the uniform legislation

Neither the preliminary examination of jurisdiction to which art. 4 ERIP *bis* refers, nor the judicial review of art. 5 of the same, can be applied to these "insolvency proceedings". In fact, the judicial body (court clerk) receiving the notifications under art. 5 *bis* LCon is not receiving a "request to open insolvency proceedings". Note that there is no court intervention even in the case of homologation proceedings under the 4th additional provision, but in an advanced stage of the proceedings, and challenge to the homologation - to which the seventh paragraph of said additional provision refers to - cannot include an *ex post* review of the jurisdiction deriving from the COMI. The same can be said of the challenge brought against the mediated settlement agreement under art. 239(2) LCon. Aside from that, there is no recourse to the safeguard remedy under art. 4(2) ERIP *bis* because there is no trustee in insolvency.

Other provisions of ERIP *bis* sit uncomfortably with Spanish pre-insolvency proceedings. These atypical proceedings can hardly entail effects such as those provided in art. 7 of the regulation. In order to be able to talk of effects on contracts, individual enforcements, provable claims, rules related to voidness or avoidance of detrimental actions, offsetting, security located abroad, etc., insolvency proceedings must have been opened. It is obvious, for instance, that within the proceedings under art. 71 *bis*(1) there is no "effect", other than the (relative) creation of a safe harbour against avoidance actions. It is questionable even that the "immunity" of third-party rights in rem (i.e., security), to which art. 8 ERIP *bis* refers, makes any sense when what is at issue is not the enforcement of security as such, but the eventual attachment to secured claims in the context of collective proceedings such as those under the 4th additional provision LCon. The same can be said of the effects on arbitral proceedings to which art. 18 ERIP *bis* refers, and so on.

The essential principle of automatic recognition regulated in arts. 19, 20 and 32 ERIP *bis* cannot be applied to theses proceedings as in respect of these one cannot aptly talk of a judgment (i.e., court decision) opening insolvency proceedings. The rules relating to trustees in insolvency (arts. 21, 22, 23) and the concomitant institutions dependent on the existence of these trustees (for instance, cooperation and coordination in concurrent proceedings involving company groups, cooperation and coordination between trustees, etc.) cannot be applied to theses pre-insolvency proceedings.

The "opening" of the secondary proceedings under arts. 3(2) and 36 ERIP *bis* is absurd if the object of such proceedings is a pre-insolvency

[1] I owe this sharp observation to my colleague Alberto Díaz Moreno.

remedy such as an early composition with creditors or a homologated refinance agreement. And it is equally absurd that a "process" similar to that provided in art. 71 *bis*(1) LCon, opened in a country other than the debtor's COMI, could be considered secondary proceedings for the purposes of ERIP *bis*. But it is also odd that coordination such as that envisaged in arts. 36 *et seq.* ERIP *bis* could take place with the opening of a pre-insolvency negotiatory process in the jurisdiction of the debtor's COMI concurrent with the opening of insolvency proceedings *in strictu senso* under art. 3(2) ERIP *bis*; among other reasons because, by definition, there is no room in main proceedings for "proceeds" distributable to local creditors. The opening at the COMI venue of negotiatory restructuring proceedings sits at odds with the opening in another jurisdiction of secondary proceedings with liquidating effects. Even if the "main" pre-insolvency proceedings included something akin to a trustee in insolvency, said trustee could not give the local creditors the "undertaking" to which art. 36 ERIP *bis* refers. The only rules that would make any sense for "secondary" proceedings of this kind would be those contained in art. 38(3)(I) and (III), 38(4), 46(1), 47 and 51 ERIP *bis* - which in fact presuppose the *de facto* non-opening of secondary proceedings or their closure -, although such converging solutions will almost never be possible as they necessarily depend on the existence of a trustee in insolvency.

The whole delicate construction of institutional cooperation designed by arts. 41, 42, 43, 57, 58 and 61 ERIP *bis* becomes senseless and impracticable in the pre-insolvency proceedings to which art. 1(c) ERIP *bis* refers to.

4. Actual usefulness of the regulatory changes

In all honesty, the inclusion of these proceedings within the harmonised regulation has no relevance other than to stress that such atypical proceedings are also subject to the law of the COMI and that both the jurisdiction of the court and the governing law follow the universality criteria appertaining to classic insolvency proceedings. With this, ERIP *bis* is limiting itself to say *who has jurisdiction* to conduct these negotiatory parainsolvency proceedings and to hold - which is no small thing - that the law governing these proceedings is the *lex forum concursus* and not the, eventually different, material law governing, also eventual, "renegotiable" contracts.