Alert | Restructuring & Insolvency

Spain, September 2022

ENACTMENT OF THE LAW AMENDING THE RECAST INSOLVENCY ACT

The Spanish Parliament's extraordinary plenary session of August 25, 2022, has passed a law amending the recast Insolvency Act, which amendment will enter into force 20 days after it is published in Spain's Official State Gazette, the *"BOE"*.

This new law, after suffering numerous amendments as a bill, establishes major changes in the area of insolvency, and it incorporates into the Spanish legal system the guidelines established by Directive (EU) 2019/1023 of the European Parliament and of the Council, dated June 20, 2019, on preventive restructuring frameworks.

Below we provide a summary of the main features introduced by this law:

1. Amendment of the Insolvency Act's Book II on "Pre-Insolvency Law". Introduction of the so-called "Restructuring Plans".

The new law abolishes the previous pre-solvency instruments (refinancing agreements and out-of-court payment agreements), and introduces what are referred to as "restructuring plans"; a new pre-insolvency instrument. These plans include restructuring measures that can affect both liabilities and assets, as well as the sale of all or part of a company.

The purpose of the reform is to enable the debtor or creditors to act at a stage of difficulty prior to that contemplated in the previous legislation. The new law refers to such stage as "**probable insolvency**", which is considered to exist when it can be objectively expected that the company won't be able to comply with its upcoming obligations over the next two years on a regular basis if a restructuring plan is not agreed upon.

Through this change the law intends to make said instruments more effective, by allowing the restructuring to be performed earlier; thus improving its likelihood for success.

The main features of these restructuring plans include:

i. The possibility that, with few exceptions, they may be applied to any type of creditor, not only financial creditors;
ii. The possibility that, once the plan has been approved by the court, its effects may apply to dissenting creditors within the same class, to entire classes of creditors, or even to dissenting partners;
iii. Establishment of the criteria to define classes;
iv. The possibility that contracts may be terminated for the sake of restructuring;
v. The possibility that contracts with executive directors or senior management can be suspended or terminated, if that is necessary to successfully complete the restructuring;
vi. Suspending the directors´/administrators´ legal duty to promote the company's wind-up due to losses during the time the effects of notifying the start of negotiations are still in force.
vii. Protection against potential future actions to terminate transactions that are necessary to successfully negotiate the plan.
viii. Creation of a figure referred to as the restructuring expert

.

2. Introduction of a special single and compulsory proceeding for micro-companies that are in a situation of both probable insolvency and imminent/current insolvency.

The Act defines micro-companies as those, which employed an average of less than 10 workers and have an annual turnover of less than 700,000 euros (or liabilities of less than 350,000 euros) during the year prior to the request for the commencement of this proceeding, based on the balance sheet closed in the fiscal year prior to the application date. Individuals may also be considered as micro-companies. They too will be eligible for the

new "second chance proceeding" which releases the party in question from the obligation to pay outstanding debts.

With the introduction of this special proceeding, the legislator has sought to reduce costs, eliminate unnecessary formalities and reduce the participation of professionals and institutions that are not essential, or whose cost is not voluntarily assumed by the parties.

Among the special features that characterize this proceeding, the following stand out:

i. lawyers or court attorneys are not compulsory, except for the debtor.
ii. the preferential use of predetermined standardized electronic forms that are accessible online and free of charge.
iii. the general elimination of in-person hearings and their substitution by virtual hearings. Matters shall be resolved, with exceptions, via written proceedings and shall not be suspensive in nature.
iv. the proactivity of the parties, which implies that the adoption of specific measures or access to certain information must be requested by the interested parties and,
v. the use of liquidation platforms with free and universal access.

This special proceeding provides for a three-month non-extendable negotiation period, with suspension of individual enforcements, during which time the party may choose between a continuation plan or the rapid liquidation of the company if the insolvency is imminent or currently exists. If the appointment of an insolvency administrator is not requested, the liquidation may be carried out by the debtor itself.

The basic foundation of this proceeding is the veracity of the information provided. Its concealment or manipulation, or the provision of incorrect documentation will be cause for the party to be declared guilty. The classification section shall only start if the micro-company is to be liquidated; it will not take place in all cases, only those where the persons entitled to do so request it. Opening the qualification section will not require the liquidation work to have been completed, as it can be carried out in parallel with the proceedings.

Due to the need to develop the elements on which this special proceeding is based, the new law does not establish its entry into force until January 1, 2023.

3. Amendment of the "second-chance proceeding" (the proceeding that exonerates the party from paying outstanding debts).

The Act regulates a merit-based exoneration system in which the good faith of the insolvent debtor continues to be the cornerstone for the exoneration of all debts, except for those exceptional cases that cannot be exonerated, where the exoneration is no longer conditioned to the payment of a certain type of debts or to the fact the party unsuccessfully attempted an out-of-court payment agreement.

Therefore, with some exceptions (e.g., debts for alimony, public law debts, or debts arising from criminal offenses), the exoneration is extended to all insolvency debts and debts claimed against the available assets.

The law establishes two types exoneration, which are interchangeable:

(i) Exoneration with liquidation of the available assets; or

(ii) Exoneration without prior liquidation and with a payment plan, the duration of which is reduced to 3 years, notwithstanding the fact it may be extended to 5 years in specific cases.

4. Express regulation of the proceeding for the sale of productive units, both in the pre-insolvency phase (as part of the restructuring plan), throughout the insolvency proceedings and particularly in what is referred to as the "pre-pack", which consists of preparing an application to have the insolvency declared upon presentation of an offer to acquire one or several production units with the assistance of an independent expert appointed by the judge.

Characteristic features of the "pre-pack" are highlighted below:

i. The possibility that, prior to filing its application to be declared insolvent, the debtor may request the competent judge to appoint an independent expert who will obtain offers for the acquisition of one or more productive units.

ii. The possibility for the debtor to submit its application to be declared insolvent together with a binding written offer to acquire one or more productive units.

iii. The offer must contain a commitment on the part of the bidder to continue or restart the business of the productive unit or units for at least two years. If the acquirer breaches this commitment, any affected party may claim compensation from the acquirer for damages caused.

iv. Once the application to be declared insolvent has been filed with the binding offer, the Act establishes a regulated proceeding with new deadlines. Any interested party may submit alternative proposals to the initial offer.

v. If several bids are submitted, the judge will select the most advantageous for the interest of the insolvency proceedings and employees' bids may be prioritized, provided that such bid is in the interest of the insolvency proceedings.

5. Introduction of mechanisms to streamline and make the general insolvency proceedings more efficient.

The following are some of the measures established to expedite such proceedings:

- Shorter deadlines to voluntarily declare insolvency and for the processing of applications to be declared necessarily insolvent.

- The effectiveness of the inventory and provisional creditor lists to initiate the term to submit agreement proposals or to file the classification report.

- The establishment of legal liquidation rules that eliminate the obligation to file a liquidation plan.

The following measures have been introduced to improve the efficiency of the proceeding:

- The use of the "pre-pack" mentioned above.
- A system whereby creditors monitor the proceedings, in cases where there are no assets.
- Increased number of acts that can be terminated, and
- Clarification of which credits are essential to maintain and liquidate the available assets.

6. Introduction of "early warning" tools to encourage the debtor to adopt measures.

Of the tools included, the following can be highlighted:

i. The creation of self-diagnosis systems so that companies can confidentially determine whether they are in a situation that could evolve towards insolvency.
ii. The establishment of public, free and confidential advisory services for companies in difficulties.

7. Regulation of the regime applicable to the public guarantees granted to face the pandemic and the war in the Ukraine.

The Eighth Additional Provision clarifies the regime applicable to these guarantees, with respect to which the following points stand out:

i. Credits derived from public guarantees will be considered as financial credit for all the purposes set forth under the Insolvency Act, including the creation of classes and the exoneration of outstanding debts.

ii. Such credits shall be ranked as ordinary credit, without prejudice to the existence of other guarantees granted to the main secured credit.

iii. The representation and defense of the credits that were based on such guarantees shall be the responsibility of the relevant financial institutions, which will act for and on behalf of the Spanish Government. However, the Act contemplates certain limitations with respect to: the content of the restructuring plans; the continuation or agreement proposals if they could affect such credits; as well as the need to obtain prior authorization from the Spanish Tax Authority's Collection Department before voting in favor of restructuring plans containing debt deferrals, instalment payments and discharges.

Finally, it should be noted that the changes mentioned are not the only ones contained in the new law. Through additional and final provisions, the new Act includes mandates aimed at reforming or approving the Regulations of the Insolvency Administration, the Regulations of the Public Insolvency Registry, the application forms for the declaration of voluntary insolvency, the electronic platform for the liquidation of assets, and the forms for the special proceeding for micro-companies. The new Act also repeals or amends several precepts of the Commercial Code, the Civil Code, the Civil Procedures Act, the Companies Act and the Mortgage Act, among others.

Regarding its **applicability** and **enforceability**, in general the new law states it will be applicable to the requests for insolvency proceedings that are filed any time after the date the Act becomes enforceable, as well as to the insolvencies declared once the Act is in force.

In turn, the new law will be applicable to the filing of any notices to initiate negotiations, to the negotiation of restructuring plans, and to the application to have such plans approved, once the Act is in force.

Click **here** to access the full text of the publication in the BOE of the Law 16/2022, of 5 September, reforming the revised text of the Bankruptcy Law approved by Royal Legislative Decree 1/2020, of 5 May, for the transposition of Directive (EU) 2019/1023 of the European Parliament and of the Council, of 20 June 2019.

For more information:

José Luis Yus
Joseluis.yus@bakermckenzie.com

Laura Camarero
Laura.camarero@bakermckenzie.com

Rocío González
Rocio.gonzalez@bakermckenzie.com

Baker McKenzie Madrid, S.L.P.
C/ José Ortega y Gasset, 29
Madrid 28006
España
Tel: +34 91 230 4500
Fax: +34 91 391 5149
www.bakermckenzie.com