The EU Restructuring Directive: how member states are progressing with transposition

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With the deadline for domestic transposition of the European Restructuring Directive having passed this weekend, McDermott Will & Emery partner **Timothée Gagnepain** and associate **Lucille Madariaga** in Paris discuss how it has been eagerly awaited – and yet is likely to be postponed for at least a year – in most EU member states.

In this article, we provide a snapshot on how member states are progressing or not with the adoption of the EU Restructuring Directive.

The stated objective of Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks is to remove obstacles to the exercise of fundamental rights, which result from differences between national laws, and procedures concerning preventive restructuring, insolvency, discharge of debt and disqualifications.

The scope of the Directive includes three key sections: common principles on the use of preventive restructuring frameworks and early warning tools with a view to preventing insolvency, which is the main building block of the Directive; procedures aimed to discharge debt for individual debtors in order to allow entrepreneurs to benefit from a second chance; and targeted

measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt in order to reduce the length and cost of procedures in member states.

While EU legislation on insolvency and restructuring has been mainly limited to cross-border recognition and cooperation, the new Directive clearly aims at harmonising the future landscape of the European restructuring market, and erasing the differences that exist between the local laws in setting minimum standards. As it is the fruit of numerous political compromises, some leeway is still being offered to the member states.

The text of the Directive was in part a reaction to the phenomenon observed for companies in a financial crisis to restructure their debt under the equivalent of the Scheme of Arrangement, which offers the possibility of implementing a debt restructuring on the basis of a majority decision of creditors.

It was noted that some European countries did not offer any efficient possibility for restructuring outside of an insolvency procedure. This situation was not satisfactory in the eyes of the European Commission as insolvency procedures have their associated drawbacks such as destruction of value and a general disincentive to investment especially in member states where debtors' interests/pursuit of the operations/preservation of jobs are regarded as prioritised over creditors' prospects. As a result, offering consistent treatment to restructuring finance was a top priority.

In this respect, and according to a communication from the Commission, "the enhancement of preventive restructuring frameworks would ensure that action is taken before enterprises default on their loans, thereby helping to reduce the risk of loans becoming non-performing in cyclical downturns, and mitigating the adverse impact on the financial sector".

To address this situation and meet its objectives, the Directive made it mandatory for member states to offer a "preventive restructuring framework" for companies in a financially distressed situation. Member states were required to transpose the Directive's provisions in their respective insolvency and restructuring domestic laws before 17 July 2021 (Article 34 "Transposition" of the Directive).

There were exceptions for specific provisions to be complied with from 17 July 2024, such as the use of electronic means of communication for the filing of claims, submission of restructuring or repayment plans, and notifications to creditors; or from 17 July 2026 for things like use of electronic means of communication for lodging challenges and appeals.

As of today, and according to the EU tracker set up by the Commission (updated as of 21 May), only a few member states have already implemented the text of the Directive in their national insolvency frameworks, including the Netherlands, Greece, Germany and Hungary. Others seem to be on track to do so like Austria and Denmark).

However, a majority of EU members have already requested an extension of the initial deadline as a derogation. Member states that "encounter particular difficulties" in the implementation process are able to benefit from a maximum of one year's extension of the implementation period, subject to prior notification to the Commission before 17 January. States that have taken advantage of this include Ireland, Poland, Cyprus, Croatia, the Czech Republic, Belgium, Italy, Portugal, Slovakia, Romania and Bulgaria.

As for the countries that did not request an extension to the deadline, little information is publicly available – however delays in the transposition are expected in France, Luxembourg, Finland and Sweden. With respect to France, rumors say that the final text will not be adopted until autumn 2021.

These delays in the implementation of the Directive into national law are allegedly attributable, depending on the member states, to the length of the legislative debates and much to-ing and fro-ing between various institutions. In France, a large consultation of restructuring professionals initiated by the French Ministry of Justice may also have impacted the initial timetable set up by the French government.

The covid crisis has also played its role and definitely turned the political (including elections) and legislative agenda on its head. Whereas corporate bankruptcies were set to rise in the context of the covid crisis, and despite the pressure to show results in the context of looming insolvencies in Q2/Q3 2021, EU countries may have chosen to prioritise enacting covid-response emergency measures on the health, economic, social and fiscal fronts, instead of speeding up the adoption of the restructuring and insolvency reform.

As underlined by professionals, adequate implementation of restructuring procedures could alleviate the burden on the court system, offer more restructuring opportunities for viable enterprises and help minimise the impact of the crisis – and of the post-crisis – on the financial systems.

It is interesting to note that Germany has been one of the model pupils among the member states regarding implementation of the Directive. The implementation of the Directive into German law came into effect on 1 January and required the member state to create a completely new legal framework for preventive restructurings.

In France, the transposition of the Directive is not expected to be such a game changer, as France already has very effective pre-insolvency processes. The major change required by the Directive will be the introduction of more extensive rules on classes of creditors. At present, only two creditors' committees exist in France (in addition to the bondholders' assembly, if applicable) in the context of safeguard and recovery proceedings, but not in pre-insolvency procedures. The possibility of using cross-class cram-down will also be a completely new mechanism and is the most anticipated contribution of the new Directive.

Professionals will have to wait and see what happens in the next chapter. To be continued ...

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