EUROPEAN
COMMISSION

Brussels, 7.12.2022
SWD(2022) 395 final

COMMISSION STAFF WORKING DOCUMENT

IMPACT ASSESSMENT REPORT

Accompanying the document

Proposal for a Directive of the European Parliament and of the Council

harmonising certain aspects of insolvency law

{COM(2022) 702 final} - {SEC(2022) 434 final} - {SWD(2022) 396 final}

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Glossary

Term or acronym	*Meaning or definition*
BCA	Business Continuity Act
BORIS	Beneficial ownership registers interconnection system
BRIS	Business Registers Interconnection System
CMU	Capital Markets Union
COMI	Company's centre of main interest
CSR	Country Specific Recommendations
DRI	Directive on Restructuring and Insolvency (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)
EAPO	European Preservation Order Procedure
EBA	European Banking Authority
EBRD	European Bank for Reconstruction and Development
ECB	European Central Bank
ECOFIN	Economic and Financial Affairs Council
EIR	European Insolvency Regulation (Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings)
ELD	Environmental Liability Directive
ESRB	European Systemic Risk Board
EU	European Union
GDP	Gross Domestic Product
HLEG	High Level Expert Group on Sustainable Finance
IMF	International Monetary Fund
IP	Insolvency practitioners
IRI	Insolvency registers' interconnection
ISSG	Commission's inter-service steering group
JRC	Joint Research Centre
MS	Member State
MSE	Micro and small enterprises
NFC	Non-financial Corporation

NPL	Non-performing loans
OECD	Organisation for Economic Cooperation and Development
RSB	Regulatory Scrutiny Board
SDG	Sustainable Development Goals
SME	Small and medium-sized enterprises
TFEU	Treaty on the Functioning of the European Union
UNCITRAL	United Nations Commission on International Trade Law
WB DB	World Bank Doing Business

1. INTRODUCTION

1.1. Political context

It is a well-established view among stakeholders, researchers, international institutions and policy makers[1] that the significant differences in insolvency rules across Member States constitute an important barrier to cross-border investments and a key obstacle to further economic integration.[2] The European Central Bank (ECB) as well as the International Monetary Fund (IMF) recurrently flagged that tackling the divergence in national insolvency rules is key to achieving progress on the Capital Markets Union (CMU). The IMF "….identifies three key barriers to greater capital market integration in Europe: transparency, regulatory quality, and insolvency practices.[3] [..] As the EU seeks to build an integrated capital market, how best to regulate the sector and improve insolvency processes become key questions."[4] According to the ECB "where insolvency and judicial frameworks are more efficient, risk-sharing through both capital and credit markets is higher [..] This empirical research finding shows that it is important to address the major shortcomings and divergence between insolvency frameworks which persist at the European level. This would require taking measures beyond the draft Directive on Insolvency, Restructuring and Second Chance".[5] Furthermore, multiple think tanks and other international bodies concluded on the significance of divergences in insolvency rules as an obstacle to cross-border investment.[6]

Regulators and market participants singled out differences in insolvency practices among the three most important barriers[7] to market integration in a survey carried out by the IMF (2019) on the benefits of the CMU and the obstacles towards its realisation. The empirical analysis undertaken by IMF identified that convergence in insolvency regimes would yield the largest contribution to three key metrics of financial integration: higher cross-border asset holdings, a reduction in cross-country differences in corporate funding costs and improved risk-sharing across the EU Member States.[8] Annex 4, Section 4

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[1] See, for instance, the Five presidents report (5-presidents-report_en.pdf (europa.eu), European Parliament resolution of 9 July 2015 on Building a Capital Markets Union (2015/2634(RSP)) and of 8 October 2020 on further development of the Capital Markets Union (CMU) (2020/2036(INI)).

[2] Similar to the degree of economic integration being measured by the level of cross-border trade, cross-border investment flows are a standard measure of capital market integration, with higher flows being indicative of a better economic integration among Member States.

3 The two other important policy triggers to cross-border investment (in addition to national insolvency regimes), such as regulatory quality and transparency of data, are addressed by other Commission initiatives (e.g. report on the operation of the European Supervisory Authorities and the proposal on the creation of the European Single Access Point). Nevertheless, the importance to tackle the insolvency-related barriers would remain irrespective of progress made on these other policy initiatives.

[4] Quoted from IMF (2019).

[5] Quoted from ECB (2018). "More efficient and harmonised insolvency laws and regulatory frameworks for equity investments, including addressing the debt-equity bias in taxation, can improve certainty for investors, reduce costs and facilitate cross-border investments, while also making risk capital more attractive and accessible to companies", ECB (2022).

[6] See for example, CEPS (Valiante, 2016), Bruegel (Demertzis et al. 2021), DIW (Bremus and Kliatskova, 2019). See also Demmou et al. (2021) for the perspective of the OECD.

[7] See IMF (2019a, 2019b).

[8] Taken at face value, the IMF analysis suggests an improvement of the recovery rate by one standard deviation (difference between Italy and Germany) would lead to a 24% increase in cross-border asset holdings, reduce the dispersion in corporate funding costs by 6% for unlisted firms and by 2% for listed firms, and increase risk-sharing through the capital and credit channel from 24% (in the baseline scenario) to 53%. For more details, see Annex 4 and in particular Figures A4.25 and A4.26.

provides more details on the statistical analysis done by the IMF, ECB and academic researchers about the impact of more efficient and alligned insolvency rules on cross-border investment and risk sharing.[9]

The Commission's first Action Plan on building a CMU[10] in 2015 argued that "convergence of insolvency and restructuring proceedings would facilitate greater legal certainty for cross-border investors". In 2015, the European Parliament adopted a resolution[11] where it called to ease cross-border investment and indicated that for the CMU to work smoothly, insolvency rules must be made to work better in a cross-border context. This led to the adoption of the Directive on Restructuring and Insolvency in 2019, which pursued targeted harmonization in the specific areas of pre-insolvency measures and debt-discharge procedures. Since it did not cover rules governing insolvency proceedings, the expert group[12] set up by the Commission and tasked with informing policy choices for the 2020 Capital Markets Union Action Plan[13] emphasised that progress towards the CMU, as the integrated market for capital, requires addressing further the inefficiency and divergence of insolvency regimes across Member States.[14] Similar recommendations were also put forward by a number of expert groups, organised by Member States and industry representatives.[15]

The CMU Action Plan from 2020[16] announced that the Commission would take a legislative or non-legislative initiative for minimum harmonisation or increased convergence in targeted areas of non-bank corporate insolvency law to make the outcomes of insolvency proceedings more predictable.[17] The Council Conclusions (ECOFIN) of 3 December 2020 on the Action Plan encouraged the Commission to deliver on this initiative.[18] In April 2021, Eurogroup concluded that national reforms of insolvency regimes shall progress in coherence with parallel work streams led by the EU

[9] The empirical approach used in economic studies to demonstrate the impact of differences in insolvency regimes on cross-border investment follows the spirit of gravity models, which are a standard tool to analyse the determinants of international trade flows, see Portes/Rey (2005) for the seminal application on cross-border capital flows, Hartmann et al (2018), IMF (2019), Kliatskova and Savatier (2020).

[10] COM/2015/0468 final

[11] European Parliament resolution of 9 July 2015 on Building a Capital Markets Union (2015/2634(RSP))

[12] High Level Forum on the Capital Markets Union (2020).

[13] COM/2020/590 final.

[14] A similar perspective is adopted in IMF and ECB publications: "differences in European restructuring and insolvency regimes will persist after implementation of the Directive, despite its goal of harmonization. The Directive shows that harmonization of insolvency laws, particularly important in the context of the Banking Union and the Capital Markets Union is a complex challenge", Garrido et al. (2021); "further harmonisation of general legal frameworks would be desirable. [...] In particular, market participants would find it easier to invest in firms located in different Member States if core elements of insolvency regimes, such as the definition of insolvency triggers, avoidance actions and the ranking of claims, were harmonised at best-practice levels", de Guindos et al. (2020).

[15] See also the reports by Next CMU set up by seven Member States, by Markets4Europe set up by financial institutions.

[16] COM(2020) 590 final.

[17] The subsequent Capital Markets Union Communication of 25 November 2021, under its Action 11 entitled "Making the outcome of cross-border investment more predictable as regards insolvency proceedings", the Commission announced that "it would propose an initiative by Q3 2022 that would seek to harmonise targeted aspects of the corporate insolvency framework and procedures."

[18] Council Conclusions on the Commission's Action Plan, doc. nr.12898/1/20 REV 1. These Conclusions were confirmed by the Euro Summit statement of 11 December 2020, Doc. nr. EURO 502/20.

institutions, which were undertaken in the CMU Action Plan.[19] The European Parliament reiterated again in 2020 that for the CMU to work smoothly, insolvency rules must be made to work better in a cross-border context.[20]

1.2. Scope of the initiative

This initiative covers business non-bank insolvency procedures and does not include insolvency procedures for banks and consumers. The banks' bankruptcy proceedings and recovery and resolution are governed respectively by the Winding up Directive and by the Bank Recovery and Resolution Directive[21] and Single Resolution Mechanism Regulation,[22] together with national liquidation law. Member States have national laws to deal with the bankruptcy of consumers, which are excluded from the scope of this initiative because of the limited cross-border dimension. Consumers do not typically raise funds from cross-border creditors and consumer bankruptcy procedures do not significantly contribute to the key objectives of the CMU.

The intiative aims at a targeted harmonisation of substantive insolvency rules. The initiative excludes policy intervention on preventive restructuring of corporations, as well as on other matters that are covered by the Directive on Restructuring and Insolvency (DRI)[23]. The intiative nonetheless includes the aspects of restructuring and reorganisation proceedings where relevant to debtors in insolvency. The scope of DRI carves out traditional insolvency law (with very minor exceptions), covering only situations of pre-insolvency and post-insolvency. The DRI deals with the debt discharge of failed entrepreneurs only to the extent it is relevant to answer the question on when and how an entrepreneur, who has become insolvent, can make a fresh start after insolvency proceedings. Section 1.4 clarifies the relationship between the DRI and this initiative.

1.3. Key insolvency concepts

Insolvency proceedings aim at ensuring the orderly winding down or restructuring of companies or enterpreneurs in financial and economic distress (i.e. that have been declared insolvent).[24] These are compulsory and collective procedures that take over the

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[19] Doc. nr. EURO 502/21. Similarly, the statement of the Euro Summit meeting of 25 June 2021 confirmed that "structural challenges to the integration and development of capital markets, particularly in targeted areas of corporate insolvency laws, need to be identified and addressed"

[20] European Parliament resolution of 8 October 2020 on further development of the Capital Markets Union (CMU): improving access to capital market finance, in particular by SMEs, and further enabling retail investor participation (2020/2036(INI)).

[21] Directive 2001/24/EC, Directive (EU) 2019/879 of the European Parliament and of the Council of 20 May 2019 amending Directive 2014/59/EU as regards the loss-absorbing and recapitalisation capacity of credit institutions and investment firms and Directive 98/26/EC. As part of the acquis, the ranking of claims in the bank creditor hierarchy was partially harmonised to ensure a common approach enhancing legal certainty in the event of resolution and insolvency.

[22] Regulation (EU) No 806/2014 of the European Parliament and of the Council of 15 July 2014 establishing uniform rules and a uniform procedure for the resolution of credit institutions and certain investment firms in the framework of a Single Resolution Mechanism and a Single Resolution Fund and amending Regulation (EU) No 1093/2010.

[23] 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.

[24] 'Insolvency' or 'insolvency proceedings' have become the more usual terms in international documents (see UNCITRAL Legislative Guide on Insolvency Law) and in the relevant EU policy instruments in the last three decades as opposed to 'bankruptcy' or 'bankruptcy proceedings'. The former ('insolvency

contractual enforcement of claims against the insolvent debtor, which would be otherwise exclusively left to the individually agreed enforcement mechanisms between a given counterpart and the debtor. This section provides a general overview of central concepts whereas Annex 5 describes the main features of insolvency systems in the EU Member States in detail. [25]

The proceedings typically include tools that ensure a timely declaration of insolvency, so that it does not affect the possibility to either restore the going concern or to ensure a cost-effective liquidation, as well as tools to maximise the recovery value of the company's assets being liquidated.

The main insolvency features relate to:

1. Governance of the proceedings;
2. Tools to recover asset values from the liquidated company;
3. Tools to distribute recovered values among creditors.

The governance of proceedings involves actions, such as defining when a business should be declared insolvent, and therefore should be subject to insolvency proceedings. It, for example, includes the obligation of directors to file for insolvency in due time before depleting the value of the company's assets (e.g. to avoid the situation where directors make large pay-outs to themselves and other employees of the company). The governance of proceedings also cover the institutional aspect: notably, if the proceedings are run before a court or another competent authority, or if an insolvency practitioner is appointed to steer the procedure and administer the estate.

The insolvency regime may also include several tools to ensure proper identification of the debtor's assets and recovery of their market value. These tools may include (i) transaction avoidance tools, i.e. actions to challenge past transactions that have been concluded to deprive creditors of the debtor's assets; (ii) pre-pack liquidation, i.e. the possibility to conduct negotiations on the sale of the company or its parts as a going concern before insolvency filing with the deal finalised in insolvency, to avoid significant value destruction due to protracted insolvency proceedings, or (iii) access rights to asset registries, to ensure proper tracing of the company's assets.

Finally, the value distribution tools of an insolvency regime include tools that govern the orderly allocation of the recovered value of the company's assets among creditors. Such distribution tools may for example include a pre-determined creditors' ranking that establishes the order of priority among various types of creditors, providing ex-ante clarity to creditors about their chances to recover value in case of insolvency and avoiding a lengthy case-by-case assessment based on court discretion in insolvency. Another tool is creditors' committees that ensure that all represented creditors' views are heard in insolvency, leading to a better coordination among creditors and more efficient

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proceedings') is generally understood as a broader term, including all types of in-court or out-of-court procedures which address collectively the financial distress of a debtor. The term 'bankruptcy' is narrower, usually connected to the judicial declaration of the insolvent state of the debtor and implies a traditional court proceeding. Irrespective of these differences, this Impact Assessment Report uses the terms as intercheangeable with each other.

[25] Further sources for descriptions of insolvency systems in the EU Member States are McCormack et al. 2016, Steffek 2019, Deloitte/Grimaldi 2022. Information per Member State is also available in the e-justice portal (https://e-justice.europa.eu/447/EN/insolvencybankruptcy).

decision making (lack of coordination among creditors often leads to disruption in insolvency cases).

A business is part of a complex web of relationships with suppliers, investors and creditors, employees, clients, public authorities (e.g. tax and social security authorities) etc. All of these groups are direct or indirect providers of financing and creditors of the business. The opening of insolvency proceedings directly affects the rights and positions of all these stakeholders. The rights of each type of creditor and some of their incentives differ in the event of an insolvency. Insolvency law is further strongly linked to questions of property law, labour law and freedom of economic activity.

From the perspective of the CMU, the outcome of insolvency proceedings and the allocated recovered value therein is of particular importance to the supply of capital and credit in the economy and particularly to providers of financing to companies. When deciding on their offers, providers of financing consider the future risk of the company becoming insolvent and the value of recovered assets for the price that they will charge for the capital offered to that company. Recovery values, recovery time and the judicial costs of insolvency proceedings are all affected by differences in national insolvency laws that ultimately influence this risk assessment and thus have bearing on the willingness to invest and provide financing across borders and on the terms of such financing.

Banks as the most common type of lenders to businesses often enjoy a senior creditor status and hence a privileged treatment in insolvency. Since the market share of other financial investors and inter-company loans has been increasing over the last years, the recovery value of the insolvent businesses' assets in an insolvency case is critical not only for banks, but also for other providers of equity and debt financing. Furthermore, value recovery could also be relevant for other companies such as suppliers, including many SMEs, which often suffer (disproportionately more than larger companies) from their trade partner becoming insolvent (often leading to what is known the *insolvency domino effect*).

Finally, public authorities are creditors in insolvency cases because of due tax or social security contributions. Often tax claims enjoy a privileged treatment in creditors' ranking. Furthermore, employees, who are in a vulnerable situation in insolvency as they may lose their jobs, enjoy special privileges in some systems in relation to due wage claims.[26]

The longer insolvency proceedings last, the bigger the adverse effects on the value that can be recovered in a liquidation ("melting ice cube" phenomenon).[27] Moreover, any judicial proceedings, including insolvency proceedings, are associated with costs. Complex judicial proceedings are associated with very high costs (including in particular

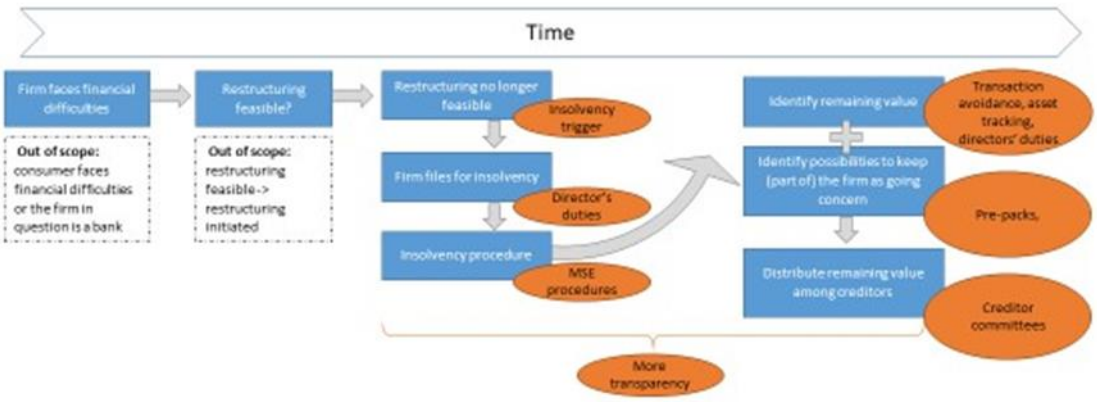
[26] The insolvency experts interviewed in Deloitte/Grimaldi (2022) stated that "Employees are in general well protected in the EU. […] Outside of insolvency regulations, governments pay the dues to employees and then become creditors of insolvent company".

[27] The recovery value will generally be smaller than 100%, but it is often not zero because, even if the borrower is insolvent, there may still be assets with a positive value. The "melting ice cube" phenomenon stipulates that the recovery value is not a fixed, exogenously determined amount, but that it tends to decline the longer the duration of the process. This is because beyond the depreciation of physical assets such as machinery over time, their value deteriorates if they are not used. Moreover, business lines that may still be viable on their own become less valuable if business relationships are interrupted.

the costs related to insolvency practitioners (IPs) who often have to be appointed in insolvency proceedings). For SMEs, the costs of proceedings can be so high, that very little or nothing is left for allocation to creditors after paying the costs. The impossibility to pay for the costs remains to be a major reason why in many cases proceedings are not even opened for SMEs, depriving them of orderly liquidation.

Figure 1 presents a visualisation of central decision points during the insolvency process.

Figure 1: A stylised perspective of the different steps in insolvency procedures and critical elements that determine their outcome



1.4. Economic context

Efficient and harmonised insolvency rules underpin the efficient allocation of capital, economic recovery from recessions and thus also economic growth.[28] In contrast, lengthy and inefficient insolvency procedures undermine economic growth by preventing capital reallocation from businesses with low profitability and high indebtness. Such businesses are investing less and are less likely to pursue innovative activity, which slows down the diffusion of technical progress and ultimately the growth potential. Capital allocation is impaired because economic resources locked in distressed entities (zombie companies) are not available for more productive uses. Banks' exposure to bad loans impairs their capacity to provide credit to new business.[29]

Insolvency rules impact on economic activity not only if a company needs to wound down and the remainings of the estate be distributed to its creditors. The expected recovery value, time and costs have an impact much earlier by affecting to what extent and under which conditions companies can get access to funding they need for their operations and growth. As further detailed below, inefficient insolvency procedures and divergences in procedures across Member States discourage the supply of cross-border funding, as evidenced by a high home bias in portfolio investment and a low proportion of cross-border credit.

[28] See Annex 4 for empirical studies in support of the arguments made in this paragraph.
[29] The more uncertain and lengthy the enforcement of non-performing loans, the stronger the incentive of banks to evergreen non-performing loans at the expense of credit to new customers.

The number of corporate insolvencies in the EU is in the range of 120,000 to 150,000 per year.[30] Data shows a substantial decline in bankruptcy declarations in 2020, which is primarily due to the public support measures during the COVID-19 crisis. Many more businesses cease to exist in the EU each year, which suggests that a substantial number of businesses are wound down without recourse to public insolvency procedures.[31] The introduction of debt moratoria and other means helped companies and entrepreneurs overcome the Covid-19 induced economic downturn at the expense of increasing the debt level in the corporate sector and the creation of a larger number of businesses exposed to debt overhangs.[32] While many observers anticipated a pronounced increase in corporate bankruptcies, it has not yet materialised.[33] It is however not excluded that it may still occur in the future, especially since the energy price shock and supply chain bottlenecks have increased the likelihood of a severe slowdown of economic growth in the EU. Accordingly, the IMF cautioned in its assessment of the euro area's economic recovery prospects that "Insufficient efforts to address labor market rigidities, debt overhang, and inefficient insolvency processes could impede efficient reallocation of resources, thus leading to significant labor market hysteresis, low productivity growth, and sizable economic scarring." [34] Although the proposed changes to insolvency rules will not be in place to support adjustment to and recovery from the current economic shocks, the latest economic developments demonstrate the vulnerability of the EU economy to sizeable economic shocks and distress. If and when future shocks hit the EU economy, corporate adjustment and the winding-down of insolvent firms should imperatively take place under more efficient and better-aligned insolvency rules in the EU, which suggests a need to act as soon as possible.

There is currently no information about the share of insolvency cases in which cross-border creditors are involved, neither for intra-EU nor for creditors from third countries. However, the data on the share of cross-border exposure of the EU companies may be seen as proportionate to the (potential) share of cross-border bankruptcy cases. It can hence allow for an approximation.[35] This data suggests that a significant number of all insolvency proceedings in the EU - 10%-20% are likely to involve claims of cross-border creditors[36]. This number should, however, not be interpreted as implying a low importance of insolvency rules for cross-border investors: the current level of cross-border investment (which may be subject to potential cross-border insolvency proceedings) is impaired by the existing cross-border obstacles, including those on divergent and inefficient insolvency regimes. It is, thus, likely to underestimate the true level of importance of cross-border insolvency proceedings, once these obstacles are

[30] See Annex 2 for a review of data sources and more information about the economic context. Eurostat collects statistics on the number of bankruptcies and companies' deaths, which are however not comparable because of differences in coverage. It does not publish bankruptcy numbers to account for differences in definitions, methodologies and structures across Member States.
[31] See Annex 4 for a more detailed discussion on the number of insolvency cases and business exits.
[32] For a quantification of the number of "zombie" firms in the euro area, see the ECB May 2021 Financial Stability Report,
[33] See ESRB (2021).
[34] see IMF (2022).
[35] It should be noted that this is an underestimation (a lower bound), as the foreign exposure only captures the direct cross-border aspects of a company's exposure. However, cross-border investors may also operate via domestic legal entities and therefore be affected by insolvency proceedings in a similar way.
[36] The term cross-border creditor is used in this impact assessment as synonym to cross-border investor.

removed (including via this initiative).[37] More details on economic context are discussed in Annex 4, Section 1.

1.5. Legal context

1.5.1. The limited scope of prior EU action

The intiative covered by this impact assessment seeks to increase the convergence of substantive insolvency rules of the EU Member States. It is different in terms of its objective and scope from any existing EU law. This section sets out how the EU law developed in the areas of pre-insolvency (preventive restruturing), insolvency and post-insolvency (second chance) over the course of the last years and where the current intiative fits in this context.

The Union started to legislate in the area of insolvency about twenty years ago. In the beginning, the EU did not aim at creating the convergence between the domestic substantive insolvency frameworks. Rather it intended to ensure a smooth coordination and cooperation between the national regimes in cases of cross-border insolvency. The EU **Insolvency Regulation** (EIR, first adopted in 2000, recast in 2015) was adopted on the legal basis for judicial cooperation in civil and commercial matters (Article 81 TFEU).[38] The EIR introduced uniform rules on international jurisdiction and applicable law that – for cases of cross-border insolvency – determined in which Member State the insolvency proceedings have to be opened and which law is to be applied to the questions at hand. In parallel, there were uniform rules that ensured that the judgments taken by the courts having jurisdiction in these cases are recognized, and if needed, enforced in the territory of all Member States. The EIR has no impact on the content of national insolvency law. It determines the applicable law but does not prescribe any features or minimum standards for that law. Therefore, it does not address the divergences across the Member States' insolvency laws (and the resulting problems and costs).

The approach of judicial cooperation hence did not comprehensively address the issues that are relevant from the perspective of cross-border investment. Accordingly, the EIR only allowed cross-border investors to establish which law would be applicable in the event of an insolvency of a debtor, but it left unchanged substantial divergences in national insolvency rules. These differences continued to weigh on cross-border investors' ability to anticipate the outcome for value recovery in case of insolvency in another Member State and hence impair cross-border investment and, more generally, capital market integration in the EU.

[37] A similar scale of insolvency proceedings with cross-border elements may be estimated from the proportion of outstanding foreing debt claims of MSE companies in the EU. According to the Flash Eurobarometer survey carried out in June 2016 among small and medium sized enterprises in the [then] 28 EU Member States, on average, 17% of those companies had debt claims against foreign debtors over 2015 fiscal year. However, in some countries this proportion was much higher: 49% in Luxembourg, 45% in Slovenia, 31% in Austria. Half of the companies with foreign debt claims say foreign debt claims represented at least 6% in their 2015 turnover. Flash Eurobarometer, Report Insolvency, no. 442, 2016, para 1 and 2. The survey data was used in the Commission Impact Assessment Accompanying the Proposal for a Directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures, SWD (2016) 357 final, p. 45.

[38] Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings.

The first Action Plan on building a CMU[39] of 2015 led to the adoption of the **Directive on Restructuring and Insolvency** in 2019. The DRI pursued targeted harmonization in the specific areas of pre-insolvency measures and debt-discharge procedures but not in relation to the rules governing insolvency proceedings *per se*. It obliged Member States to introduce preventive restructuring procedures with certain minimum standards and to provide fair debt discharge for failed entrepreneurs[40].

The preventive restructuring procedures are only available to debtors in financial distress **before they become insolvent**, (i.e. when there is only a likelihood of insolvency) and are based on the fact that there is a much greater chance to save ailing businesses when tools for restructuring their debts are accessible for them at a very early stage and before they become definitively illiquid. These rules do not bring about any harmonisation of the rules governing insolvency. The minimum standards on the second chance for failed entrepreneurs, set out in the DRI, do not address the way insolvency proceedings are conducted either. They rather relate to the discharge of debts for insolvent entrepreneurs as a consequence of insolvency and could be described as a regulation of **post-insolvency effects**. Nevertheless, the DRI includes a few cross-cutting rules that also affect insolvency matters to a very limited extent. These rules contain very general high-level principles concerning specific topics (the training of judges, some professional standards for insolvency practitioners and the means of communication in insolvency proceedings) which were so horizontal in nature that it would have been artificial to regulate them for pre-insolvency and post-insolvency proceedings but not for insolvency proceedings.

The initiative covered by this impact assessment does not seek to reopen the elements already covered by the DRI. Beyond these limited elements, the DRI does not harmonise any substantive insolvency law; its restructuring rules are expressly applicable only on the condition that the company in question is not yet insolvent. As a result, the substantive insolvency laws of Member States are currently not approximated at the EU level and as acknowledged by the EIR remain "widely differing".[41] The limited scope of the DRI can be explained by the fact that pre-insolvency restructuring proceedings were considered important in order to create frameworks allowing to preserve value by avoiding insolvency proceedings where possible in a situation where such frameworks were previously entirely absent in many Member States. The relative novelty of such pre-insolvency proceedings to a considerable number of national legal orders made this an adequate topic for a first step of harmonising substantive law in the broader area of insolvency law because of the reduced number and sensitivity of clashes with the long-established principles under national law. This first step having been achieved, the initiative covered by this impact assessment aims at taking the next step by seeking the convergence of the rules governing insolvency where a debtor cannot be returned to viability in pre-insolvency restructuring but has to enter into insolvency proceedings.

[39] COM/2015/0468 final.

[40] The deadline for the transposition of the Directive on Restructuring and Insolvency is July 2022 and a review is foreseen for 2026.

[41] Recital 22 of the EIR: "This Regulation acknowledges the fact that as a result of widely differing substantive laws it is not practical to introduce insolvency proceedings with universal scope throughout the Union. […] This applies, for example, to the widely differing national laws on security interests to be found in the Member States. Furthermore, the preferential rights enjoyed by some creditors in insolvency proceedings are, in some cases, completely different. […]"

Figure 2 provides for a schematic representation of the coverage of the areas (pre-insolvency, insolvency, post-insolvency) and actors by the existing legal acts, as well as identifying the existing gap in EU law (substantive rules on insolvency proceedings).

Figure 2: Aspects and areas relevant to insolvency regulated and not yet regulated in EU law

ASPECTS / AREAS	CROSS-BORDER PROCEDURAL ASPECTS	SUBSTANTIVE ASPECTS		
		PRE-INSOLVENCY	INSOLVENCY	POST-INSOLVENCY
PROCEE-DINGS	**EIR** - Applicable law -International jurisdiction - Recognition of the effects of opening insolvency and of further judgements taken in the course of the insolvency proceedings - Group coordination proceedings	**DRI** - Debtor in possession - Stay of individual enforcement actions -Restructuring plans - Cross-class cramdown - Protection for new financing and interim financing - Duties of directors	***NOT YET REGULATED AT THE EU LEVEL*** *- Material elements of insolvency (transaction avoidance, asset tracing, duties of directors (and liabilities) of companies to file for insolvency, pre-packs)* *- Procedural elements of insolvency (opening of insolvency proceedings, special insolvency rules for micro- and small enterprises)* *- Distributional elements of insolvency (ranking of claims, creditors' committees)*	**DRI** - Debt discharge proceedings - Reasons for disqualification
ACTORS TARGETED	**EIR** - Powers of insolvency practitioners in cross-border situations	**DRI** - Training of judges - Training of insolvency practitioners - Supervision and remuneration of practitioners		**DRI** - Honest entrepreneurs - Possibility for Member States to extend to consumers

1.5.2. The divergences between national laws on key features of insolvency law

There are important differences across Member States with respect to various aspects of substantive insolvency law. This section illustrates some of these differences across the relevant elements as a basis for the discussion of why they emerged as problem drivers in Section 2.3 of this impact assessment. More details on differences across Member States are provided in Annex 5.

Rules on **transaction avoidance** to protect the insolvency estate against undue transactions and thus ensuring the preservation of value for creditors exist in all EU Member States. Apart from few exceptions, they cover a broad range of reasons and recipients and define a maximum timeframe for the retrospective period for voidable

transactions[42]. However, the features of national systems diverge considerably. In certain Member States, like France, Germany, Poland, Portugal and Sweden, all legal acts are subject to avoidance rules, regardless of whether they were performed by the debtor, the defendant or a third party, provided that they are detrimental to the general body of creditors. By constrast, in other Member States, like Czechia, Malta, the Netherlands, Slovenia and Spain, only transactions by the debtor that have disadvantaged the general body of creditors are covered.[43]

Different EU regulations enable taking evidence and other **asset tracing** and recovery measures in civil or commercial matters across EU Member States[44], although excluding the insolvency proceedings. The EIR does not specifically address the issue of asset tracing in the context of cross–border insolvency proceedings. It provides that the powers of insolvency practitioners are governed by the *lex fori concursus*[45]. Thus, the EU landscape is very fragmented in this respect and each Member State has its own rules and entrusts the insolvency practitioners with different powers in respect to the asset tracing.[46]

In relation to **directors' duties and liability in the vicinity of insolvency**, only a duty to convene a meeting exists in EU company law (2017 Company Law Directive[47]) but there is no obligation to take a decision on re-capitalizing or liquidating the company in difficulty. Member States take different strategies to protect creditors in the vicinity of insolvency by imposing varying duties on directors[48]. In a significant number of Member States[49], directors must file insolvency proceedings within a certain period of time of their company becoming insolvent. The time in which filing must be done, however, varies widely across the EU (e.g., "immediately" in Germany, within one month in Belgium, within two months in Spain, no express time limit in some Member States). Some Member States make it clear that in the vicinity of insolvency, the focus of directors should shift to the creditors' interest.[50] In Hungary, the change in duty involves the interests of creditors as a priority, and directors could be held liable for a form of wrongful trading. The German approach provides that the directors must call a meeting of shareholders in case of "serious loss of the subscribed capital" to take measures to safeguard both the interests of the company and its creditors. Some Member States (like

[42] Rules on avoiding certain types of transactions concluded by the management in the vicinity of insolvency (or when already insolvent) and thereby clawing back the assets concerned to the insolvency estate (for the benefit of the creditors) represent an immanent part of all national insolvency regimes.

[43] A more detailed description of the aspects of transaction avoidance, including a more detailed description of rules of Member States law in this area, can be found in section 2.1. of Annex 5.

[44] Regulation (EC) No 1206/2001; Regulation (EU) No 805/2004; Regulation (EC) No 1896/2006; Regulation (EC) No 861/2007.

[45] Art. 7 EIR.

[46] A more detailed description of the aspects of asset tracing, including a more detailed description of rules of Member States law in this area, can be found in section 2.2. of Annex 5, see in particular the Table about the powers of insolvency practitioners in the area of asset tracing across EU Member States.

[47] Directive (EU) 2017/1132 of the European Parliament and of the Council of 14 June 2017 relating to certain aspects of company law, OJ L 169, 30.6.2017, p. 46–127.

[48] In certain EU jurisdictions, the existence of a near insolvency situation does not lead to any marked change in the general duties of directors. The jurisdictions where a change is noticeable are Cyprus, Denmark, Estonia, Hungary, Ireland, Latvia, and Malta. Denmark, for example, addresses the proximity of insolvency by providing that directors must exercise special care when this situation exists.

[49] The circumstances that trigger the need for directors to file are variously described, but effectively amount to the demonstrated state of insolvency. For example, in most common law jurisdictions, there is no obligation on the directors to file proceedings if their company becomes insolvent.

[50] See mapping of the divergences in national laws in McCormack et al. (2016), pp. 44.

Italy[51]) require that, in case, of "serious loss of the subscribed capital", the board shall call a meeting and have the company decide, upon losing half of its subscribed share capital, whether to recapitalise or wind down the company's business and liquidate it[52].

When an insolvent business has to be liquidated, creditors can usually achieve a greater recovery rate if the business or a part thereof is sold as a going concern, i.e. as an operating, value generating economic entity.[53] An effective form of a sale of the business as a going concern in insolvency proceedings is the "pre-packaged sale" or '**pre-pack'**, where a non-public negotiation phase between the debtor and some possible buyers precedes the formal opening of the insolvency proceedings. Whereas the liquidation of the debtor through a going concern sale is allowed in most of the insolvency laws of the Member States, pre-pack mechanisms exist only in a handful of Member States. Those that govern pre-packs, do it differently. For example, the sale of the entire assets of a debtor on a going concern basis is only possible outside of court in France, it requires court involvement in Belgium unless the pre-pack is organised as amicable settlement. Whereas pre-pack sales must achieve the continuation of the business in France, the German rules intend to liquidate the business.

With respect to **opening of insolvency**, there are typically two insolvency tests under national law that are used as insolvency triggers: the balance sheet test or the cash flow-based test. Different Member States use the general cessation of payments (cash-flow) test and the balance sheet test in different combinations to establish a commencement standard. Regardless of the causes that lead to insolvency, there is no unambiguous definition of "insolvency" across all Member States (numerically identifiable and therefore easily predictable or monitored)[54]. Hence, one can currently expect as much as 27 different answers under each Member State law or the question whether a business is (in)solvent, or likely to be insolvent that is whether or not it is making a profit sufficient to provide a return to the business owner while also meeting its commitments to business creditors or where it has sufficient cash resources to sustain itself through a period when it is not returning a profit. Moreover, in some Member States (e.g. the Netherlands) the court has relatively wide discretionary powers in assessing whether the debtor has ceased to pay its debts.

In most Member States, large companies and MSEs are treated alike and there are no special procedural alleviations to cater for the specific situation that **micro- and small enterprises (MSEs)** face when they are in financial distress. Small- and micro enterprises do not even have access to liquidation proceedings in a number of Member States, as in most cases such debtors have no or only very few assets left when becoming insolvent, which circumstance barres them from the opening of insolvency proceedings (i.e. Austria, Germany, Greece and Italy) or results in an immediate termination of

[51] Article 2474 Italian Civil Code.

[52] A more detailed description of the aspects of directors' duties and liability in the vicinity of insolvency, including a more detailed description of rules of Member States law in this area, can be found in section 2.3. of Annex 5.

[53] Recovery values tend to be lower in the alternative "piece-meal liquidation" under which individual assets of the business are sold separately.

[54] In fact, concepts such as "insolvency" or "vicinity to insolvency", as well as "crisis", which are often used in the European regulatory framework as well as in individual national laws, are not defined at EU level.

insolvency proceedings (i.e. Belgium and Spain)[55]. Simplified liquidation procedures for MSEs are available only in Czechia, France, Greece, Lithuania, Romania and Slovakia.[56]

While some features of the **ranking of claims of creditors** are common to all Member States (e.g. the prioritization of secured over unsecured creditors), national systems are substantially divergent[57]. Almost all the Member States ensure a preferential treatment of secured credit[58], but the position of *secured creditors* vis-à-vis other claims, specifically those relating to *taxes and/or employee rights* varies significantly. In the Netherlands – historically known to be a 'creditor-friendly' jurisdiction[59] – secured creditors are granted a strong position in respect of their claims as (in principle) these outrank other creditors (including those with a right of preference).[60] Only in specific exceptions may other claims take priority over secured claims. The most important example of this is the preference that is granted to the Dutch tax authorities for certain categories of tax debts over certain movable assets located on the premises of the debtor.[61] In turn, in France – a jurisdiction historically known for being debtor-friendly[62] – secured claims are (in principle) outranked by other claims.[63] In Spain claims concerning salaries, taxes and social security withholdings are granted (in said order) a status of 'general privileged claims'[64], however, these are still outranked by 'insolvency' claims, and special privileged claims[65] (i.e., secured with *in rem* security over specific collateral (e.g., mortgage or pledge). On the other hand, in Germany certain categories of secured creditors do not fall within the ranking order since they shall benefit from an exclusive right over the economic value of the assets and, in practice, rank ahead all other creditors. Creditors entitled to separate satisfaction are completely excluded from the concept of insolvency creditors: they are granted a priority right of satisfaction and have the possibility to pursue their claims outside the rules of the relevant insolvency legislation[66], i.e., in normal civil proceedings. In relation to specifically protected interests, Germany,

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[55] A more detailed description of the aspects of special insolvency regime for micro- and small enterprises, including a more detailed description of rules of Member States law in this area, can be found in section 3.2. of Annex 5.

[56] See McCormack, G. et al. (2016).

[57] In particular, a number of Member States afford particular privileges to tax and other governmental claims. Some Member States give a priority or even super-priority ranking (trumping all other claims including those of secured creditors) to the claims of employees (unpaid wages). Furthermore, there are significant differences also with regard to the treatment of "new financing" in subsequent insolvency proceedings.

[58] It is a fundamental principle of insolvency law that pre-insolvency entitlements of creditors should be respected by insolvency and restructuring rules unless there are legitimate grounds to a post-commencement redistribution of value, see Wessels et al. (2017)

[59] See Brown Rudnick (2020).

[60] Article 3:279 of the Dutch Civil Code.

[61] Wet van 30 mei 1990 inzake invordering van rijksbelasting (Invorderingswet 1990 (IW 1990), Act of 30 May 1990 on the collection of state taxes (Collection of State Taxes Act (CSTA)), article 21.

[62] However, the implementation of the RDI in France may lead to a shift towards a more creditor friendly insolvency framework. On this matter, see Podeur (2021) and Golshani et al, page 14.

[63] First and foremost, a portion of employees' pre-petition claims benefits from a super-senior status ("superprivilège des salaires") [Arts. L622-17, French Code of Commerce]. Additionally, pre-petition tax claims also rank ahead pre-petition secured claims, For more information on the national insolvency framework in France, see Talbourdet and Gumpelson (2021).. For more information on the national insolvency framework in France, see Talbourdet and Gumpelson (2021).

[64] Article 280 of the Spanish Insolvency Act, Real Decreto Legislativo 1/2020,.

[65] Article 270 of the SIA.

[66] Sec. 47 of the Insolvenzordnung (Insolvency Statute) of 5 October 1994 (BGBl. I p. 2866), as last amended by Article 35 of the Act of 10 August 2021 (BGBl. I p. 3436).

for example, keeps workers in the same rank as all other unsecured creditors because its law and social safety net shelters workers from the consequences of their employers' insolvency[67].[68]

In the vast majority of jurisdictions a **creditor committee** may/must be appointed and its general role is to safeguard the interests of creditors. The amount of input that committees have in the administration of the insolvency, however, varies greatly. This difference affects the actual extent of creditor involvement in the proceedings. For example, while in some Member States they are merely carrying out an advisory role (e.g. in Denmark), in other Member States (e.g. in Greece) the functions of the committee are, principally, to support and supervise the insolvency practitioner (and even control the insolvency practitioner) and give consent for some actions to be taken by him/her. Similarly, in Austria for certain important transactions (e.g. sale of the business), the consent of the creditor committee is a precondition for their validity. In other Member States, such as Germany, for transactions of particular importance, such as entering into a loan contract with considerable burdens on the insolvency estate, the insolvency administrator needs the approval of the creditor meeting or of an appointed creditor committee. In Romania, the creditor committee can request the removal of the debtor's right to manage its affairs.

2. PROBLEM DEFINITION

2.1. What are the problems?

Insolvency rules are fragmented along the lines of national insolvency systems (see section 1.5).[69] They thus deliver different outcomes characterised by different degrees of efficiency across Member States in terms of the time it takes to liquidate a company and the value that can eventually be recovered (see Figure 3). This leads to a pronounced length of insolvency procedures, and a low average recovery value in liquidation cases (see Table 1). Differences in national regimes also create legal uncertainty as regards the outcomes of insolvency proceedings and lead to high information and learning costs for cross-border creditors.

Low recovery values, long insolvency procedures, administrative costs of the procedures matter not only for the efficiency of a company's liquidation. Even more important is that these three factors and the uncertainty surrounding them determine the magnitude of the risk premium that creditors factor in when they undertake an investment. A high risk premium increases the cost of capital for the corporation and, if the risk is particularly high, dissuades investors to provide credit and cross-border investors to consider investing abroad.

[67] The general lesson to be drawn from this example is that liens should not be granted by insolvency law, but by those laws - social security law, labour law, etc. - that are responsible for that particular protection (as is the case in Denmark, for example).

[68] A more detailed description of the aspects of ranking of claims, including a more detailed description of rules of Member States law in this area, can be found in section 4.1. of Annex 5.

[69] For a comparison of descriptions of the features of insolvency systems in the EU Member States that are discussed in this impact assessment, see Annex 5, for more comprehensive comparisons of insolvency systems, see McCormack et al. (2016), Steffek (2019), Deloitte/Grimaldi (2022).

2.1.1. Costly and lengthy (national and cross-border) insolvency proceedings lead to low recovery values

If companies are liquidated, the recovery value is usually a low proportion of the initial investment. Whereas investors may be able to estimate the likelihood of insolvency, they face uncertainty about the consequences of an actual insolvency, which will depend to a considerable extent on the length and complexity of the individual case. Moreover, the predictability of outcome in insolvency cases and of recovery rates for cross-border creditors also depends on the level of discretion exercised by courts and IPs in insolvency cases. Insolvency laws do not offer adequate guidance on how the discretion should be exercised by courts (and insolvency practitioners).

Divergences in insolvency laws may increase uncertainty to such an extent that investors are not able to predict, quantify and manage the risks that affect their investment. This exposure to uncertainty will be mirrored in a higher risk premium demanded and in consequence higher funding costs for the corporate sector or even in greater reluctance to do business with foreign companies at all. Beyond the impact on risk premium, a lengthy insolvency proceeding reduces the present value of the expected investment returns, as the opportunity cost for creditors and investors of allocating these funds in other more profitable investments increases with passing time. Uncertainty about the possible value or time of recovery is an important factor for financial investors that need to generate returns or obtain additional refinancing if an investment is not redeemed in time to manage their liquidity needs.

A protracted time to recover some value may even lead to creditors becoming at risk of becoming insolvent themselves, leading to a possible cascade of defaults. This could be the case, especially for business partners that are not financial institutions, but rely on outstanding payments for the delivery of their products and services.

The scale of the problem is expected to be large: recovery values and recovery time determine recovery rates, which in turn determine the level of cross-border asset holdings[70] and risk sharing.[71] The insolvency experts interviewed in Deloitte/Grimaldi (2022) stated that they would expect sizeable gains in terms of lower costs and shorter duration of proceedings from the initiative subject to this impact assessment, pointing to considerable inefficiencies in the current insolvency regimes. Nevertheless, a comprehensive quantification of these inefficiences is not feasible due to a lack of data on recovery rates and on the degree to which they are influenced by the length and complexity of insolvency procedures.[72] Even many banks struggle to report recovery rates for non-performing loans despite credit provision being their daily business.[73]

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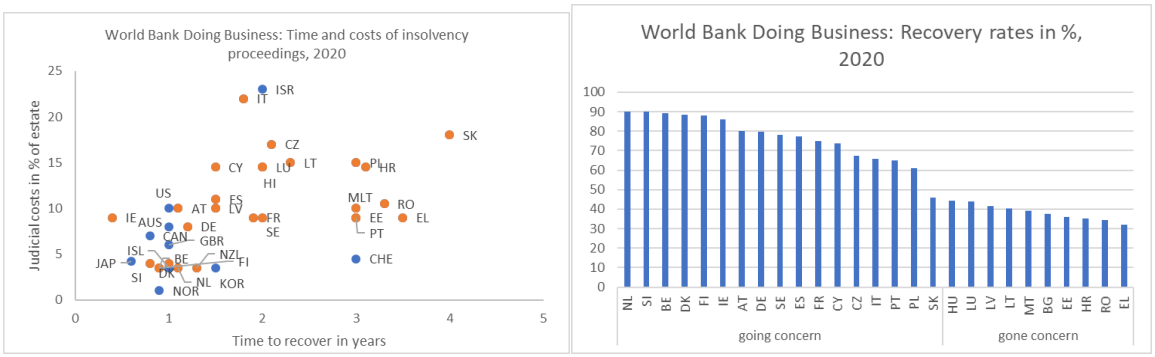
[70] See Annex 4, specifically the sections presenting the results of IMF (2019) and Bremus and Kliatskova (2018). Since these studies use the recovery rate as indicator of the strength of the insolvency regime and demonstrate a significant link between the recovery rate and measures of cross-border investment, one can derive that any policy measure that improves recovery rates would also foster cross-border investment.

[71] ECB (2018) and IMF (2019) show a significant correlation between recovery rates and the extent risks are shared across Member States through the capital and credit channel, with improved cross-country risk sharing being one of the economic benefit of the Capital Markets Union.

[72] Standard pricing models used in finance offer little help in estimating recovery values and recovery rates since these rely on discretionary decisions and timing of insolvency practitioners and courts. Theoretically, it would be possible to calculate the expected recovery rate as a function of the yield difference of a corporate bond (or credit default swap) to the safe interest rate and the expected likelihood of default. In practice, this requires determining two unknown, namely the likelihood of default and the recovery rate,

Figure 3. Time and costs of insolvency proceedings and recovery rates



Source: World Bank Doing Business Report.

Despite considerable efforts to produce data on the outcome of insolvency proceedings, little data is available to date.[74] Annex 4, Section 2 explains the different data sources and their limitations. The analysis conducted in this impact assessment relies primarily on two sources: The World Bank Doing Business indicators[75] presented in the charts above and data from the benchmark study carried out by the European Banking Authority (EBA) in 2020.[76] The two sources, however, contain rather different data. In the World Bank exercise, insolvency experts are asked to assess the outcome of insolvency procedures based on a narrowly defined illustrative bankruptcy case[77]. In contrast, the EBA collected actual data from banks in the EU Member States on gross replacement rates, net replacement rates (i.e. after judicial costs), time for recovery and judicial costs.[78]

The World Bank Doing Business data yielded recovery rates in the case of liquidation in an EU Member State between 32 and 44 %, with an average for the Member States

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and it turns out not feasible to disentangle both without recourse to strong assumption on one of them.[73] This is evidenced by the difficulties EBA encountered in sourcing such data for its benchmarking exercise, see EBA (2020), especially the sections on data quality.

[73] This is evidenced by the difficulties EBA encountered in sourcing such data for its benchmarking exercise, see EBA (2020), especially the sections on data quality.

[74] According to the survey performed with the Member States in the process of verification of the Insolvency Recommendation as well as on the basis of the comparative law study, the overall picture is very inconsistent: currently, in certain Member States data about insolvency proceedings are not collected, in certain Member States they are collected but not necessarily in a centralised or electronic manner; in other Member States where data about insolvency proceedings are collected in a centralised and electronic manner they are not always published or are not available in an anonymised way, i.e. stay confidential.

[75] The evidential value of World Bank's Doing Business scoring is limited. The irregularities in reporting information to the World Bank were found in relation to four countries, namely Azerbaijan, Saudi Arabia, United Arab Emirates and China. These irregularities triggered the pause of the Doing Business report announced on August 27, 2020. The review process did not identify any further specific data irregularities beyond those affecting these four countries as described in this document. The methodology for scoring of insolvency frameworks has been reviewed following this incident.

[76] See EBA (2020).

[77] The first indicator aims at measuring the efficiency of insolvency frameworks by estimating the recovery rate associated with a stylised corporate insolvency case. This estimate is obtained by surveying practitioners about the most likely outcome, the expected length, and the cost of a fictitious insolvency case for a business whose main asset is a hotel. The other indicator ("strength of insolvency legislation") measures on the basis of expert judgement the extent to which the insolvency framework abides by the efficiency criteria described in Djankov et al. (2008). See annex 4 for more information on insolvency indicators.

[78] See EBA (2020), Report on the benchmarking of national loan enforcing frameworks, EBA/REP/2020/29.

concerned of 38%.[79] The recovery rate in the five best performers outside the EU was 50 to 51%.

Data from the World Bank shows that the length of insolvency procedures and judicial costs in EU Member States tend to be higher than in other OECD countries (see chart above). National insolvency experts that provided estimates for benchmark scenario used for the World Bank Doing Business insolvency indicators pointed to a range of 1.5 to 3.5 years for the duration and judicial costs between 9 and 15% for EU Member States, which compares to 1.2 years and 5% costs for the fifth best performer in the panel of non-EU countries.

The EBA benchmarking exercise on national loan enforcement in insolvency (see Table 1) found that on average it takes 3.4 years and costs 1.4% of the recovery value to enforce corporate loans in the EU. Judicial costs for SMEs loans, however, are much larger in proportion, at 3.5% of the recovery value, while their time of enforcement is about the same as for corporate loans. The EBA benchmarking exercise also found that the simple average of recovery values of corporate loans in the EU is 40% of the amount outstanding at the time of the default and 34% for SMEs.

Table 1. EU-27 EBA benchmark exercise (2020)

	Corporate loans			SME loans		
	Simple average	Weighted average	Median	Simple average	Weighted average	Median
Recovery value[1]	40.4	26.2	16.2	33.8	35.1	4.9
Time to recovery[2]	3.4	3.9	2.7	3.3	3.5	2.2
Judicial costs[1]	1.4	0.5	0	3.5	1.2	0

Source: EBA. [1] gross, as a share of the notional amounts at time of default, [2] in years, from the start of the formal enforcement status to the date of ultimate recovery from the formal enforcement procedures.

The EBA benchmark exercise also revealed substantial variations across Member States, with the average recovery time ranging from 0.6 to 7 years and judicial costs ranging between 0 to above 10%.

The pronounced differences across EU Member States, documented in the EBA and World Bank data, suggest that procedures in some Member States suffer much more from delays and result in additional costs. Both data sources also show that enforcement regimes in some Member States yield considerably less efficient outcomes than the best performers in the EU. The World Bank data suggests that the average outcome for EU Member States is less efficient in terms of recovery values, time and judicial costs than in the best performers outside the EU. It is unlikely and no analysis exists that demonstrates that these differences could be entirely explained by debtor characteristics.[80]

[79] In the World Bank exercise, insolvency experts were asked to provide an estimate for the case that the underlying firm was either liquidated or restructured. The numbers quoted are from those 10 Member States and non EU countries in which insolvency experts assumed the firm will be liquidated.

[80] One can implicitly derive that the variation in the insolvency outcome is larger than what firm or industry specific-factors suggest from those empirical studies that use firm level data and despite controlling for these factors find a significant impact of insolvency indicators on the number of bankruptcies (Fatica 2022) or funding costs (IMF 2019b).

2.1.2. Low predictability of insolvency proceedings lead to high information costs and constitute barriers to cross-border investments

Differences in legal systems across Member States fragment the single market and increase transaction costs for cross-border business:[81] "disparate national law rules may lead to higher transaction costs, especially information and possible litigation costs for enterprises in general and SMEs and consumers in particular. Contractual parties could be forced to obtain information and legal advice on the interpretation and application of an unfamiliar foreign law."[82] Already in the mid-1990s, "legal uncertainty was regarded by the European Commission as the main reason for the fact that the economic dynamics triggered by the process of European integration in the early nineties developed more slowly than expected and desired".[83] Transaction costs are caused by "(a) costs of collecting information, (b) costs of legal disputes, (c) costs of setting incentives for pushing through legal claims, and (d) other transaction costs" and these "costs are higher in international transactions than in domestic trade".[84]

Legal uncertainty and associated transaction costs could also be expected specifically in the case of differences in insolvency regimes. The divergence of insolvency regimes across EU Member States[85] discourages cross-border investments through high information and learning costs and low predictability of outcome of recovery rates. Large divergences in time to recovery, judicial costs and recovery rates among Member States suggest that cross-border investors in the single market are at a higher risk of being unable to predict outcomes of insolvency proceedings if they allocate their investment portfolio across several/different Member States.

Information costs and low predictability of the investment outcome in insolvency and recovery rates play a key role for cross-border creditors, since they need to account for all possible scenarios and so the conditions and prospects for recovery of their investments in case of failure of the company they are invested in. This aspect is even more important for unsecured funding operations, which require significant knowledge of procedures and conditions affecting recovery rates in insolvency. The higher is this knowledge, the easier and more accurate will be the calculation of loss given default and probability of default and therewith the price discovery of financial assets, which is key to the orderly functioning of capital markets.

The more dissimilar the insolvency system abroad is from that in the home country, the less can domestic experiences and those made in other jurisdictions be used to assess the expected return on a cross-border investment if the debtor becomes insolvent. The consistent finding in empirical studies is that geographical distance and clusters of legal traditions[86] are important determinants of cross-border investments. This confirms the

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[81] See Cecchini (1988) and Wagner (2005).
[82] COM(2001) 398 final
[83] Wagner (2005).
[84] Wagner (2005) provides a holistic analysis of the costs of legal uncertainty.
[85] Recital 22 of the European Insolvency Regulation: (22): "This Regulation [the European Insolvency Regulation] acknowledges the fact that as a result of widely differing substantive laws it is not practical to introduce insolvency proceedings with universal scope throughout the Union. […] This applies, for example, to the widely differing national laws on security interests to be found in the Member States. Furthermore, the preferential rights enjoyed by some creditors in insolvency proceedings are, in some cases, completely different. […]"
[86] This is covered by a dummy variable if the home or destination country follows an Anglo-Saxon, Nordic, Latin or Germanic tradition or a dummy variable measuring a common legal origin.

notion that familiarity matters, suggesting that the more similar the rules, the lower the threshold to engage and undertake the necessary due diligence.[87] Greater differences in substantive insolvency laws make it more costly to assess the risks of cross-border investments compared to those realised in a home Member State. High information barriers with respect to claim procedures increase the costs of legal advice.[88]

Recent studies presented empirical evidence that the outcome of insolvency proceedings and their respective design have a significant effect on the magnitude of cross-border investment across EU Member States. The effect is material even when using different data sources and specifications for measuring insolvency and cross-border investment.[89] The statistical support at macro level that convergence of insolvency regimes to best practices would foster capital market integration implies by inversion that inefficient and diverging insolvency regimes are an obstacle to cross-border investment. Due to the methodological difficulties of (objectively) measuring information and learning costs, the empirical research about the transmission channels is still scarce.[90] The effects of insolvency regimes on the magnitude of cross border investment should be overall comparable to those of other institutional determinants such as investor protection, accounting standards or corporate governance for which the empirical literature established a significant link to cross-border investment.[91]

While there is no data about the magnitude of information and learning costs that cross-border creditors face, these costs can be approximated through the substantial home bias in investment. Home bias describes the under-proportionate investment in cross-border equity and debt (and hence over-proportionate investment in home equity and debt). Home bias is evidenced in a large body of empirical research, and the literature attributes an important role of informational frictions and uncertainty avoidance in explaining it.[92]

2.1.3. Stakeholders' perspectives

129 stakeholders submitted replies to the public consultation on this initiative, which is a sufficiently large number to derive quantitative results about their positions.[93] These results can, however, not be considered fully representative for the EU. Stakeholders from one large Member State are over-represented, while there were no submissions from some EU Member States. Like all public consultations, there is also a self-selection

[87] While familiarity appears as a factor separate from information costs in Roque Cortez et al. (2014), empirical studies tend to cover them with similar variables.

[88] On top of other costs and risks, such as language support, translating terms, general standardisation of tools, access to information. For more, please see the interviews with insolvency experts conducted by in the study conducted by Deloitte/Grimaldi (2022) on behalf of the Commission (Annex 4, Section 3).

[89] See Annex 4, Section 4 for more details on these studies. IMF (2019) and Bremus and Kliaskova (2020) use the World Bank insolvency recovery rates and the IMF Coordinated International Investment Portfolio Survey, Kliatskova and Savatier (2020) the OECD insolvency data and the ECB Security Holdings Statistics.

[90] Wagner (2005) reports that the most widespread means to measure legal uncertainty and the underlying information costs consist in indicators that measure differences in legal institutions (such as the rule of law or insolvency indicators) or are based on surveys of risk experts or cross-border investors.

[91] See for example Giofre (20014), Poshakwalea and Thapa (2011), Ferreira and Miguel (2011). The legitimacy of using the results of these studies is supported by the finding in Jack (2018) that the World Banks' legal rights index is correlated with recovery rates.

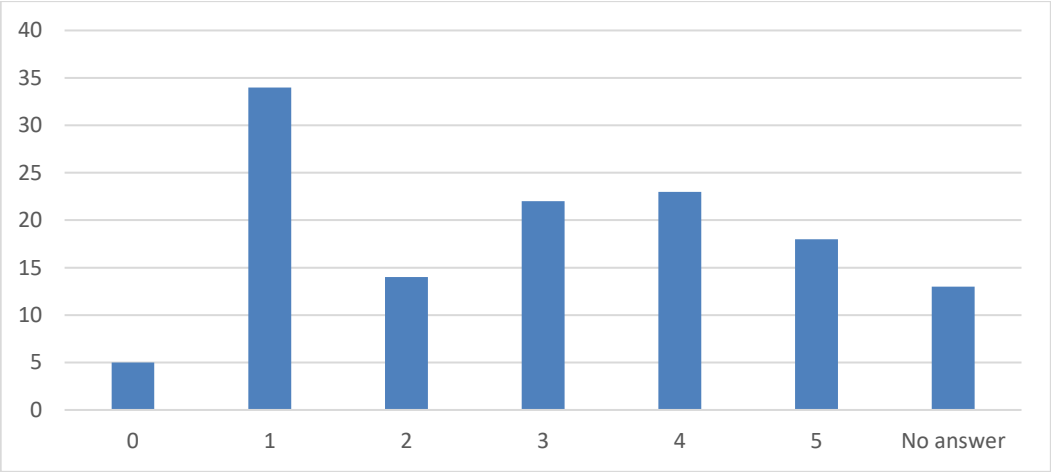
[92] See for example, Portes and Rey (2005), Aggarwal et al. (2012). Measures of home bias of debt and equity holdings are part of the CMU indicators.

[93] See Annex 2 for more details on the public consultation.

bias, implying that stakeholders for whom the issue is particular pertinent are overrepresented.

The replies to the public consultation on this initiative revealed that stakeholders find that the problem created for the internal market by differences in Member States' insolvency frameworks is serious. 54% of the respondents who provided an answer to the question perceived the problem for the internal market stemming from the divergence in insolvency rules as important, attributing a score between 3 and 5 (with 0 meaning no problem and 5 meaning an extremely significant problem).

Figure 4: Number of responses in the public consultation – Do differences in corporate (non-bank) insolvency frameworks in EU Member States pose a problem for the functioning of the internal market?



Note: 0 means 'no problem' and 5 means 'extremely significant problems'

An especially large representation of German respondents (58 out of 129) created a geographical bias in the response rate. The responses revealed a geographical split across the Northern and Southern Member States. They also showed that researchers and the business sector see a higher need for policy measures than public authorities. The views and level of ambition of insolvency practitioners and legal experts differ depending on the issue.[94]

[94] This may be explained by the fact that insolvency practitioners and legal experts provide legal advice on cross-border rules. The more aligned the rules in the EU would be, the less the need for such advice migh be in the future.

Figure 5: Average support rate in the public consultation by Member State

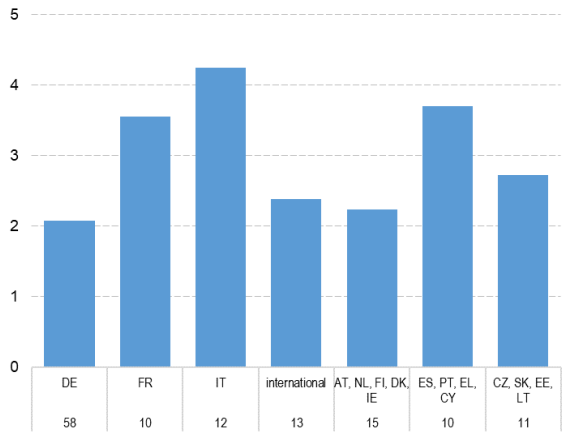
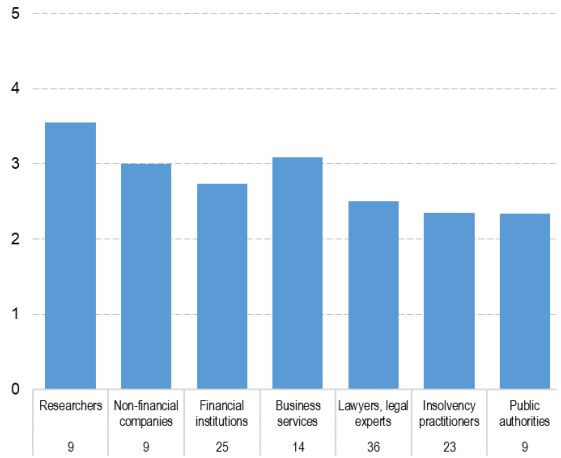


Figure 6: Average support rate in the public consultation by sector representation



Note: Average rating on a 0-5 scale with 0 means 'no problem' and 5 means 'extremely significant problems'. Number of responses on the x-axis.
Source: European Commission.

When asked for the reasons, stakeholders indicated that differences in national insolvency frameworks deter cross-border investment/lending. In a follow-up workshop with selected stakeholders, these stakeholders reported on practical difficulties resulting from the fragmentation or different performance rates of the national insolvency frameworks. These stakeholders expressed strong support for greater convergence in insolvency rules in the EU. Annex 2 provide more details about stakeholders' views.

2.2. What are the consequences?

The first consequence of lengthy, costly and very divergent insolvency proceedings is the impact on capital allocation, which is likely to be less efficient compared to the situation when insolvency regimes are more efficient and overall more similar across Member States. Creditors and investors anticipate the consequences of inefficient insolvency regimes in their decision to provide credit or to invest.[95] They will demand a higher risk premium or insist on other safeguards such as collateral, which increases capital costs for the corporates.[96] This higher risk can also discourage investors from undertaking the investment at all, limiting the supply of funding available to companies, leading to higher funding costs for corporations and, more broadly, to less efficient capital allocation in the EU economy.

The design of insolvency systems therefore has consequences for the provision (supply) of credit, capital costs and the allocation of capital. The academic literature reviewed in Annex 4, Section 4 found empirical evidence of significant adverse effects of inefficiencies in insolvency regimes on cross-border capital flows, credit provision,

[95] For a theoretical analysis of the interaction of bankruptcy rules and corporates' financial structures in terms of optimal contract design, see von Thadden et al. (2010). See Annex 4, Section 4.2 for an analysis on the impact of insolvency regimes on credit provision.
[96] Davydenko and Franks (2008) suggest that weak credit protection induces creditors to look for compensating measures, in particular to request higher collateral. See Annex 4, Section 4.3 for literature on the impact on credit conditions.

funding cost and, ultimately, the adjustment capacity of the economy, with follow-on effects on the diffusion of technical progress and productivity growth.[97] Whereas the earlier economic research found that better insolvency regimes lead to more lending to the economy in cross-country comparisons,[98] newer studies point that positive effects of more efficient insolvency regimes are better visible in funding costs or non-price credit conditions in advanced economies.[99] Annex 4 gives more details of this literature.

Since they impair cross-border investment, both differences and inefficiencies in insolvency regimes fragment the single market for capital in the EU and deter the realisation of the CMU that seeks to build an integrated market for capital in the EU. Since market practitioners consider divergence of insolvency regimes a central obstacle to cross-border investment, absence of tangible progress in this policy field could jeopardise the credibility of the overall CMU project. The studies quoted in the introductory section provide evidence that more efficient (and more converging) insolvency regimes spur cross-border investment and macroeconomic risk sharing.[100]

Finally, differences and inefficiencies in insolvency regimes can also have an impact on business relocations. Business can relocate either to declare bankruptcy and avoid paying creditors (insolvency tourism), or to gain certain advantages that would allow them to benefit from the availability of more favourable insolvency laws. In practice, however, while the possibility for the company to migrate to a different and more favourable jurisdiction may be an option in theory, this may end up being costlier and more inefficient than staying in the debtor's own jurisdiction. A recent study finds that relocation can only be an option for large companies.[101] In any event, the reduction or elimination of key differences between national insolvency laws and an enhanced degree of efficiency of insolvency regimes across the EU would remove incentives for relocations that are driven by the existing divergences.

2.3. What are the problem drivers?

The members of the expert group on insolvency, the stakeholders in the public consultation and the external contractor performing the economic study[102] in the preparation of this Report recognised the differences in certain targeted aspects of insolvency rules as drivers of the problems identified above. Insolvency tools available in these areas appear to be very different across Member States (See also Section 1.4. of this impact assessment). For several of these elements, rules are missing completely in some Member States' insolvency regimes; where they exist, their design may deliver

[97] A more efficient insolvency regime speeds up economic recovery after recessions in Jorda et al (2020), which they link to fewer zombie companies holding back productivity growth in countries with more efficient insolvency procedures. Also OECD research (McGowan, et al. 2017 and 2018) found that capital blocked in zombie companies is higher, the weaker the insolvency regime, which slows down capital reallocation, weakens the adjustment process and ultimately slows down the diffusion of technical progress and productivity growth. See Annex 4, Section 4.1 for a discussion of the effects.
[98] See Djankov et al. (2008), replicated in Uttamachandani et al. (2021).
[99] See AFME (2016) and IMF (2019) on capital costs, Davydenko and Franks (2008) and Deakin et al (2017) on non-price credit terms.
[100] "[C]ross-country risk sharing in the euro area remains quite low, highlighting the importance of policy initiatives such as the capital markets union and the completion of the banking union. [..] More efficient insolvency frameworks appear to be associated with higher risk sharing via both the capital and the credit channels", Draghi (2018).
[101] Spark, Tipik, Study on the issue of abusive forum shopping in insolvency proceedings, DG JUST 2022.
[102] Deloitte, Grimaldi (2022).

suboptimal outcomes, at least in some of the Member States. They are grouped below according to the role they primarily play in triggering various problems.[103] One driver might lead to several problems. Similarly, several drivers might contribute to the same problem and reinforce it.

2.3.1. Inadequately designed (or missing) features and large cross-border divergences on asset recovery proceedings

Some of the components of insolvency regimes help recover as much capital as possible from the insolvent company. If they are missing or not well designed, there is scope for moral hazard because the owner, debtor or director of a company may face an incentive to procrastinate on filing for insolvency ("gamble for resurrection") or to use their better knowledge of the company to redirect resources away from the estate, thereby leading to a lower value that can be distributed to creditors. Detecting whether transactions have been initiated for this purpose or whether assets are placed in hidden places allows increasing the recovery value.

Without suitable measures that govern transaction avoidance, it is difficult to claw back assets that were alienated in the vicinity of insolvency, for example transactions to benefit owners or transactions at unjustified prices. Member States have currently very different rules to govern transaction avoidance aimed at the rescission of, or the compensation for, transactions that are detrimental to creditors and had been performed prior to the opening of insolvency proceedings. Divergences among Member States go across all the key elements of transaction avoidance, such as the suspect periods, the legal acts concerned, the limitation period and so on (Grimaldi and Deloitte 2022). For example, only transactions of the debtor are considered in some Member States (Czechia, Spain, Malta, the Netherelands, Slovenia), whereas all legal acts performed by the debtor, the defendant or a third party that are detrimental to the general body of creditors are subject to avoidance actions in others (Germany, France, Poland, Portugal, Sweden). There are also divergences in the suspected periods and in the limitation periods across Member States. Such differences lead to information and learning costs in particular for cross-border investors and makes cross-border investments, especially in companies in financial difficulties, more costly.[104]

Consultations with stakeholders (see Annex 2) revealed problems related to asset tracing, especially where the asset is situated in another Member State than the one where the proceedings have been opened. Each Member State has its own rules and entrust the insolvency practitioners with different powers in respect of asset tracing. This implies that powers of insolvency practitioners may not include coercive measures if they are not provided by the applicable law, unless ordered by a court of the specific Member State or the right to rule on legal proceedings or disputes. Missing or cumbersome possibilities of asset tracing impair the capacity of courts, insolvency practitioners or other parties with a legitimate interest to determine and locate the assets, examine the revenue generated by often fraudulent activity, and follow its trail. As a "follow the money" tool, asset tracing

[103] These problem drivers are more granular than those that for example World Bank and OECD have subjected to a mapping into numerical values. While this lack of numerical indicators for granular features of insolvency regimes complicates the empirial search for evidence, Annex 4, Section 2 reports on properties for some of them that are linked to the problems and consequences elaborated above.

[104] Recovery values as measured in the EBA (2020) benchmarking exercise are however not higher in those Member States with a broader group of actors subject to rules on transaction avoidance.

is of particular significance in an insolvency context, as debtors have an incentive to remove assets from the insolvency estate.

Directors and managers' have a key role in the vicinity of insolvency. It is detrimental to the recovery value if rules are absent or ineffective that govern (i) when directors have to file for insolvency, (ii) whether their goal should shift to the creditors' interest, or (iii) whether they are liable if it is found that they acted, prior to the advent of formal insolvency proceedings, with intent to defraud creditors. Procrastination in the start of the process, including of attempts to engineer restructuring solutions early on, however, tend to reduce the recovery value.[105] Duties (and potential liability) for directors are very differently defined across the EU. In some Member States there is not even such a duty, while in others there is a duty to file within a very short timeframe or more generically in a 'timely manner'. As illustrated in Annex 5 Section 2.3, the time in which filing must be done varies widely across the EU and directors have different obligations vis-à-vis shareholders.

This divergent landscape generates additional costs, uncertainty and, hence, obstacles for investors that operate cross-border. This can be further complicated by the fact that investors can also hold directors' positions in various companies and face different obligations in companies in different Member States. This is particularly the case, in both large and small innovative companies, for very active investors with large stakes that want to be more engaged with the governance of their (invested) companies.

Recovery values are low and could be different across Member States, everything else being equal, also because pre-pack sales are not available in Member States. At present, many Member States either do not have pre-pack procedures or have very different rules regulating them. Some of those Member States that have rules on pre-packs are among those with the highest recovery rates (Denmark, Netherlands and Sweden).[106]

2.3.2. Inadequately designed (or missing) features and large cross-border divergences in the governance of insolvency proceedings

Procedural efficiency is determined by the capacity of public actors such as courts and insolvency practitioners to deal with the liquidation of a company.

Without the involvement of public actors in insolvency proceedings, the possibility of creditor runs leads to a market failure, i.e. creditors who claim first will be served first and those that claim last will receive only what is left.[107] A market failure occurs since this can lead to companies being liquidated prematurely. Since it is not rare that companies face liquidity shortages and payment difficulties, there is a risk that creditor runs lead to the liquidation of viable companies that face temporary difficulties.

The absence of lighter procedures for micro and small companies (MSEs) contributes to the workload of courts and insolvency practitioners. MSEs are often not wound down properly[108] but remain in limbo. Incentives to close their cases are distorted because the

[105] For an analysis of incentives to file for insolvency and their impact on recovery values, see for example Gurra-Martinez (2020).
[106] Three other Member States with pre-pack regimes are however not: France, Italy and Poland.
[107] See Hart (2000), Longhofer and Peters (2004).
[108] This is for example suggested by the comparison of almost 700,000 exits of businesses with less than 5 employees with about 2700 cases of corporate bankruptcy in a sample of six Member States (BE, DE, FR, NL, FI, SE) in 2019.

costs of proceedings can easily exceed the value of the estate. For MSEs, in particular, traditional long and complex liquidation procedures easily cost more money than what they are able to generate in proceeds for creditors. To allow an orderly liquidation of MSEs, some Member States already have a lighter regime, which may even avoid the launch of standard proceedings if resources are structurally limited (size of the firm). However, the picture is rather patchy across the EU and the conditions and the definitions of eligible MSEs vary considerably.[109] While France and Greece introduced simplified rules for MSEs recently,[110] MSEs for example in Austria, Germany and Italy will find their application for opening insolvency proceedings rejected if their remaining asset value is too low to cover the expenses of that insolvency proceeding.

Companies normally face financial distress some time before an insolvency procedure is initiated. From the perspective of the creditor, the insolvency trigger is therefore a determinant of the length of time s/he is exposed to uncertainty. In the absence of a harmonised definition there could be as many as 27 different answers to the question of whether a business is (in)solvent and the insolvency procedure should start, which creates high information and learning costs for cross-border creditors. In some Member States the main determinant is the cash flow, i.e. a company is declared insolvent when it cannot pay its debts as they become due. In other Member States, it is also the value of a company's liabilities on its balance sheet outweighing the value of its assets. Most Member States apply a combination of both determinants and many also require a durability criterion (See Table A5.1 in Annex 5).

2.3.3. Inadequately designed (or missing) features and large cross-border divergences on procedures for distribution of recovered values

A number of components in insolvency regimes govern the position of all types of creditors and define rules that determine the share of the value of the estate that can be paid to each creditor.[111] Their design impacts on their bargaining position and incentives of each creditor to support the resolution of the insolvency case.

Knowledge of these rules is important for investors and creditors when they decide to provide credit or to invest. Transparency and fairness of these rules is also important for those business partners of a defaulting company that became creditors through their provision of goods and services to the defaulting company. Creditors are heterogeneous. There are differences in the type of claims on a defaulting company (financial, trade credit, labour liabilities, obligations vis-à-vis public authorities). Creditors' different priority status (secured, senior, junior) generally entails high information and learning costs for (other) creditors and have a substantial impact on the recovery prospects and risk premia.

The large divergences across Member States on how distribution of recovered value is organised mean that costs are even higher for creditors acting cross-border, which may hamper their willingness to do business. Cross-border creditors will in particular need to understand what the existing rules mean for their position in the group of creditors and

[109] Thresholds for access to simplified MSE insolvency proceedings diverge: the value of the company's business needs to be less than EUR 100,000 in Greece; the company's assets can be be a maximum of EUR 5 million and creditors be less than 50 in Spain; assets need to be below EUR 300,000, gross revenues below EUR 200,000 and debt a maximum €500,000 in Italy. See Grimaldi and Deloitte 2022.
[110] 2019 and 2021, respectively.
[111] Including tax authorities and employees.

relative to preferred creditors, debtors and other stakeholders, such as employees or public authorities. They are likely to be disadvantaged, facing obstacles to coordinate with domestic creditors due to different legal regimes, language and less knowledge about the (divergent) insolvency systems and domestic actors. Creditors from third countries encounter problems identical to those of cross-border creditors within the EU.[112]

The potential drivers that contribute to determining the distribution of recovered value among the different creditors include the ranking of claims and creditor committees (in the scope of this initiative) and a few others (which are not in scope and briefly discussed in a separate section below).

The ranking of claims is of key interest to creditors since it determines the distribution of the remaining value of a defaulted company. It presents an important source of uncertainty because the impact of the ranking of creditors on the expected recovery rate is generally hard to predict for all creditors. They are a particular challenge for cross border creditors since systems are substantially divergent across Member States and the differences are not sufficiently transparent. For example, a number of Member States afford particular privileges to tax and other governmental claims (for example Italy, France, Spain). Some Member States give a priority or even super-priority ranking (trumping all other claims including those of secured creditors) to the claims of employees (unpaid wages).[113] A new phenomenon with potential impact on the ranking of claims concerns the remediation of environmental damage.[114] Given their impact on the risk premium and, hence, the cost of lending, divergences in this area may act as a significant deterrent for engagement by cross border creditors.

While creditor committees exist in most Member States,[115] different rules across Member States and limited powers and scope in some of them (see Table A5.9 in Annex 5) for creditor committees contribute to the high information and learning costs for cross-border creditors, in particular due to the difficulty to coordinate their actions during proceedings or the risk of facing hold-up problems.[116] Cross-border creditors are, in particular, disadvantaged by language barriers and unfamiliarity with domestic proceedings. Unless they hold a sizeable claim against the defaulting company, cross-border creditors are likely to face a bargaining disadvantage relative to domestic creditors. As creditors' committees provide an institutional guarantee that creditors can articulate their views in the insolvency proceedings, in particular thanks to their oversight by the insolvency practitioners, cross-border creditors may specifically benefit from this tool to compensate their disadvantages listed above. Thus, rules on creditor committees can have a decisive impact on the recovery value.

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[112] The remoteness of creditors from third countries should have an effect on where they invest. Whereas intra-EU investors often invest in neighbouring countries, extra-EU investors have an incentive to focus on large Member States to counter their information costs with higher scale economies in larger markets.

[113] For example, Cyprus, France, Italy, Lithuania, Poland.

[114] The issue is of relevance for the Environmental Liability Directive (Directive 2004/35/EC), which offers an EU framework for preventing and remediating environmental damage in accordance with the 'polluter pays' principle, as enshrined in the EU Treaties.

[115] Exceptions are Belgium, Greece, Latvia and Malta. It is of advisory nature in Denmark, limited to business reorganisations in Sweden and requires court intervention to be established if the firms is below certain size in France.

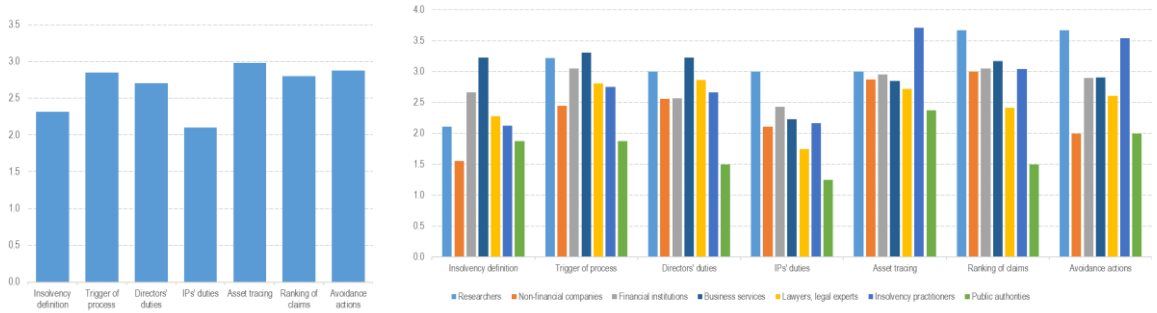
[116] Hold up problems describe when some parties block decisions that are in the interest of the group in order to gain a larger benefit for themselves.

2.3.4. *Stakeholders' views about problem drivers*

When the DRI was negotiated as well as in their replies to the public consultation, Member States reasoned that the close links of insolvency law with other areas of national law would make full harmonisation of insolvency rules not feasible at this point. Many stakeholders, however, argued that the complexity and opacity around national insolvency laws is a barrier to cross-border investments as it makes it costly to understand and measure the risk in investing in the EU. This applies to both EU as well as non-EU investors.

Stakeholders expressed divergent views in the public consultation about the importance of the different problem drivers as an obstacle to the single market.[117] For example, insolvency practitioners highlighted in particular divergent rules on asset tracing and avoidance actions as important obstacles.[118] Financial institutions identified the insolvency trigger and the ranking of claims as the key obstacles, whereas non-financial business indicated asset tracing and the ranking of claims. Firms that provide consultancy or other services to businesses flagged the insolvency trigger, directors' duties in the vicinity of insolvency and the ranking of claims as most concerning. Researchers argued that both avoidance actions and the ranking of claims needed to be harmonised, whereas public authorities generally considered the need to act on any of the proposed elements as low.

Figure 7: Stakeholder views on the extent problem drivers constitute a problem for the functioning of the single market on a scale 0 to 5, average reply in the public consultation (left-hand chart) and average per stakeholder group (right-hand chart)



Note: 0 means 'no problem' and 5 means 'extremely significant problems'.

The relevance of the different problem drivers can also be derived from the indications about their cost and time saving potential that the insolvency experts surveyed in Deloitte/Grimaldi (2022) attributed to them. The existence of cost and time saving potential suggests that current rules are not efficient. Table 2 shows how many of the insolvency experts supported measures in this area and their assessment of the effectiveness of EU harmonisation from the perspective of cross-border insolvency procedures. It suggests that foreign investors would derive benefits mainly from measures that improve asset recovery and transparency, and perhaps see less in relative terms direct benefits from common MSE regimes and creditor committees. Similarly to the results of the public consultation, German and Swedish respondents were less

[117] See section 3 in Annex 2 for a description of the methodology and more detailed results.
[118] Their overrepresentation in the panel leads to a high average rating for these elements.

supportive of wider harmonisation efforts than French, Spanish or Italian respondents.[119] Respondents from Romania and Poland were on average even more supportive than those from the Southern Europe in this survey, differing from the views of respondents from Central and Eastern Europe in the public consultation, to which neither Polish nor Romanian stakeholders contributed.

Table 2: Indications by insolvency experts about the impact of policy measures on the effectiveness of an EU regime from the perspective of cross-border creditors

	Avoidance actions	Asset tracing	Directors duties	Pre-packs	MSE	Ranking of claims	Trans-parency*	Creditor committee
Approval rate+	82.4%	85.8%	74.1%	70.0%	53.4%	61.6%	87.5%	51.6%
Score**	0.7	1.0	0.8	0.6	0.4	0.5	1.1	0.3

Note: + a % share of the 120 interviewed insolvency experts who indicated an increase in effectiveness out of all positive replies to "Considering the overall effectiveness of the cross-border insolvency procedure, as concerns the liquidation of debts and the satisfaction of the claims of creditors, please provide us your estimate of the change in the overall effectiveness determined by the introduction of EU rules" [in this area]. * A glossary of insolvency terms and of the equivalent professional figures in different jurisdictions. **. The score is defined as 0 indicating no efficiency gains, 0.5 marginal gains, 1 normal gains and 2 significant gains and likewise for negative values.
Source: FISMA with Survey data from Deloitte/Grimaldi.

2.3.5. Out -of-scope drivers

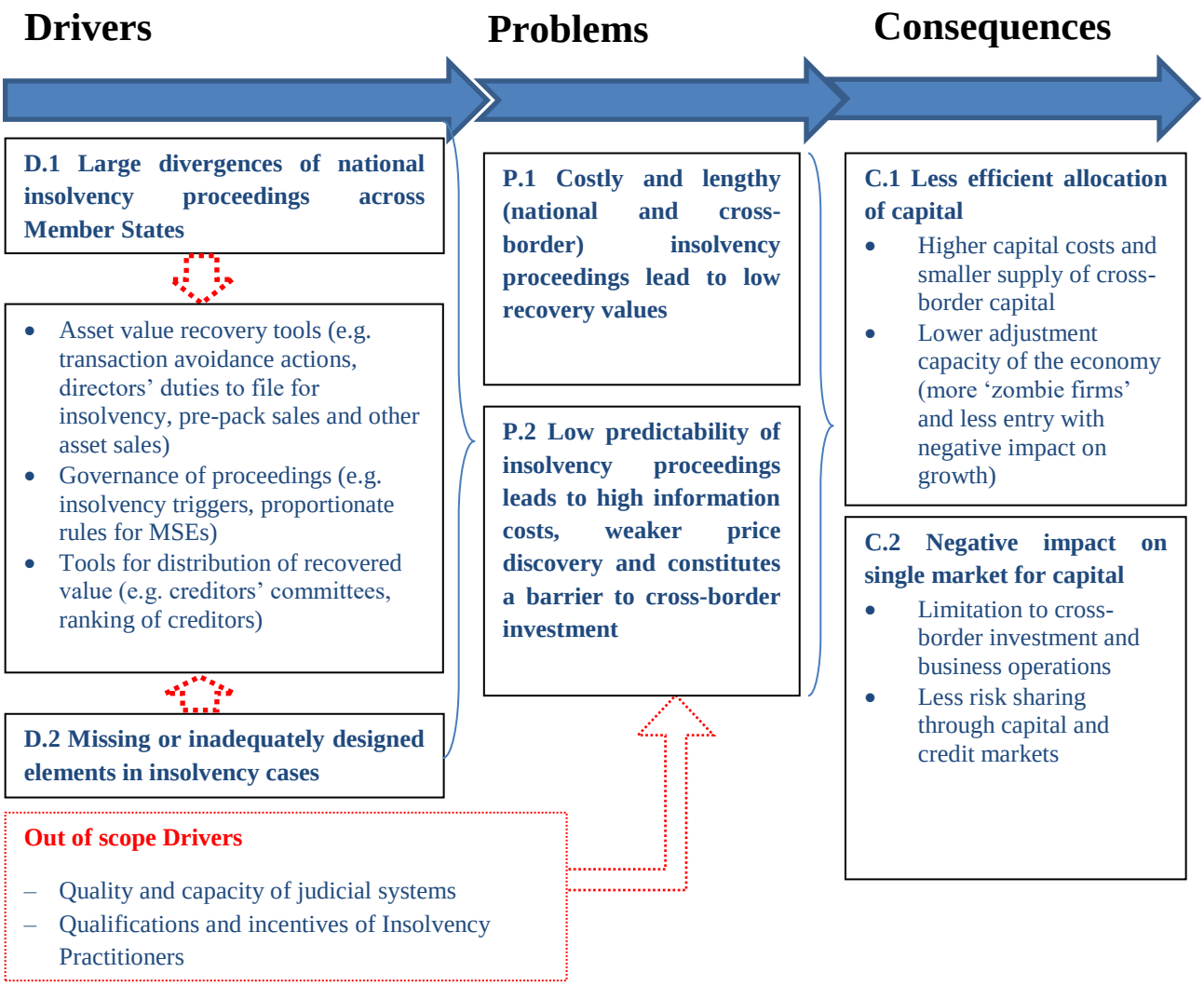
The proper functioning of the courts and the high quality of judges can significantly contribute to reducing the length of proceedings[120] and increase the ability to distinguish viable from non-viable companies[121]. The long recovery time documented above is also the result of (insufficient) court capacity.

In the same way, the qualifications and incentives of insolvency practitioners can have a significant impact on the running and outcome of insolvency proceedings. On the one hand, costs for insolvency practitioners, for example, reduce the payback to creditors and often make the opening of bankruptcy procedures non-economical for smaller companies. On the other hand, insolvency practitioners often play an essential role in ongoing proceedings. Notably, they can act on transaction avoidance and trace assets, manage the operations of the insolvent estate and influence how the debtor's assets are sold. The powers and efficiency of insolvency practitioners thus affect the length of the insolvency framework and therewith the trust cross-border investors place on the efficient treatment of their claims. The exposure of insolvency practitioners to conflict of interests, the absence of mandatory professional assurance and – possibly – standards relating to their remuneration makes them sensitive to moral hazard that can compromise their role as neutral and independent actors.

Nevertheless, despite their importance, this initiative excludes an intervention on the capacity and quality of judicial systems and qualifications and incentives of insolvency practitioners. First, major interventions to improve capacity and quality of domestic courts and insolvency practitioners adds a major complexity to the overall EU action, such as the need to have significant political support (currently lacking) for major

[119] German and Swedish respondents were particularly more negative on the effectivenss of an EU regime for pre-packs, MSEs and transparency. Swedish experts were also critical on asset tracing and creditor committees.
[120] See, for example, Kruczalak-Jankowska et al. (2020).
[121] See Ayotte and Yun (2007).

reforms of domestic judicial systems and significant investments in available infrastructures and personnel. Moreover, the Directive on Restructuring and Insolvency is already expected to lead to some convergence towards more efficient court structures and framework for insolvency practitioners. As the Directive is being transposed, it is still too early to take stock or envisage another EU intervention.



2.4. How will the problem evolve?

In the absence of an initiative on the convergence of insolvency laws, EU action would remain restricted to the few general provisions in the Restructuring Directive on insolvency proceedings concerning digitalisation, training of judges and insolvency practitioners and data collection and to country specific recommendations issued each year towards several Member States[122]. This does not leave ground to believe that action would be taken across Member States to move in the direction of a coordinated or comparable solution for the problems and problem drivers identified above (see Annex 6 for a review of progress with insolvency reforms in the Member States).

The expected phasing out of policy measures to keep distressed companies as going concerns during the Covid-19 economic downturn and the significant adjustment

[122] Recommendations in relation to insolvency frameworks to Member States within the annual European Semester exercise address only a small number of Member States and, thus, cannot achieve a consistent solution to an EU-wide problem. Maintaining the status quo will imply ongoing disparity between the national legislations on insolvency.

challenges for the economy[123] are likely to increase the number of business exits in the future.[124] The exposure of the EU economy to energy price shocks and supply-chain bottlenecks evidenced in 2022 reveal the vulnerability of the EU economy to pronounced economic shocks. Whenever these hit the economy, companies may come into conditions where their debt level turns out unsustainable or may find that changes to demand and factor costs make their business models no longer viable.[125] The baseline scenario is therefore one in which a rising number of insolvency cases will continue challenging the capacity of judicial systems. The absence of converging insolvency regimes will imply that the magnitude of cross-border investment and extent of cross-border business relationships would remain below its potential.

3. WHY SHOULD THE EU ACT?

3.1. Legal basis

Since the objective of this initiative is to ensure the functioning of the Single Market, the EU has the right to act under the Treaty. Article 114 TFEU provides a suitable legal basis for the approximation of legislation and administrative actions in Member States. The use of Article 114 is justified by problems for the functioning of the Single Market, which result from the disincentives to invest across borders (described in more details above) as a consequence of the divergences and inefficiencies in national insolvency laws.

3.2. Subsidiarity: Necessity of EU action

The functioning of the single market is in the interest of the EU and all Member States. Without EU actions, there is no mechanism to foster that elements of national insolvency regimes would become more similar over time. An important obstacle to the functioning of the single market for capital and the completion of the CMU would remain unadressed and many companies would be deprived of access to (cross-border) investment. Member States' different starting points, legal traditions and policy preferences imply that reforms at national level in this area are unlikely to lead to converging insolvency systems. Member States that assess their insolvency regime as already well-functioning may not undertake any reforms that make elements of their system more similar to those in other Member States. Among those Member States with higher recovery rates, there are only two that have undertaken insolvency reforms in the last years or committed to doing so in the recovery and resilience plans.[126] Member States that consider their insolvency system as in need of reform are likely to focus on improving elements that promise an increase of effectiveness of the national system and tailor them to their domestic preferences rather than aiming to make them more similar to those in other Member States.[127]

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[123] Including the transition to a greener and digital economy and the strengthening of the EU's strategic open autonomy. "Insufficient efforts to address labor market rigidities, debt overhang, and inefficient insolvency processes could impede efficient reallocation of resources, thus leading to significant labor market hysteresis, low productivity growth, and sizable economic scarring," IMF (2022).

[124] See ESRB (2021), OECD (Demmou (2021).

[125] See Fell et al. (2021).

[126] These are Spain and Slovenia. Further information on insolvency-related reforms in Member States is included in Annex 6.

[127] The European Insolvency Regulation "acknowledges the fact that as a result of widely differing substantive laws it is not practical to introduce insolvency proceedings with universal scope throughout the Union" (recital 22). This attests that Member States' individual action in the area of insolvency will not suffice to ensure convergence of their insolvency regimes.

Since cross-border creditors are not part of the electorate, there is a risk that national reforms will be biased towards the interest of domestic stakeholders and not place sufficient attention to the interests of and disadvantages faced by cross-border creditors.

3.3. Subsidiarity: Added value of EU action

Action at the European level is better suited to substantially reduce the fragmentation of insolvency regime and ensure convergence of targeted elements of Member States' insolvency rules towards the rules that would work well across all Member States. Rules at national level with a cross-border component, such as cross-border asset tracing, information to cross-border creditors, would be less suitable to address the needs of cross-border creditors and imply higher information and learning costs for them than if they were following a common design at EU level.

Measures at the EU level would ensure a level-playing field and avoid distortions of cross-border investment decisions caused by both lack of information about and actual differences in the designs of elements in insolvency regimes. This would help to facilitate cross-border investments and competition while safeguarding the orderly functioning of single market. Since divergences in insolvency regimes are a key obstacle to cross-border investment, addressing this obstacle will be crucial to realise a single market for capital in the EU.

EU action would act as motor of reform and help overcome policy inactivity in the Member States to address issues with core insolvency rules.[128] The options proposed respect the principle of proportionality, are adequate for reaching the objectives and do not go beyond what is necessary. They aim at striking a balance between establishing pan-European standards in targeted areas, while at the same time, leaving sufficient flexibility to Member States to adapt to local conditions and to maintain the consistency of insolvency rules with the broader national legal system.

4. OBJECTIVES: WHAT IS TO BE ACHIEVED?

4.1. General objectives

This policy initiative aims to contribute to the more efficient allocation of capital in the single market and enhance market integration under the CMU. While it cannot and will not, on its own, achieve capital market integration in the EU, it could, alongside other CMU measures (outside the scope of this initiative), contribute to the creation of more favourable conditions for better market integration.

- A first general objective is to allocate capital in the economy more efficiently, which means supporting the provision of credit to companies and improving the adjustment capacity of the EU economy as elements crucial for balanced economic growth and a highly competitive social economy. This requires accomplishing more efficient (non-bank) insolvency regimes in the Member States that are able to generate a higher recovery value of liquidated companies in a shorter time and at lower costs than at present.

[128] See Annex 6 for a review of progress with insolvency reform in the Member States in the last decase and their announcement of reforms in their recovery and resilience plans.

- The second general objective is to ensure the free movement of capital in the single market by fostering investors' trust and increasing cross-border investment, with the ultimate objective of creating a level playing field for all economic operators in the EU concerned with regards to insolvency rules regardless of their location. This demands to make the design of insolvency regimes more similar across Member States and reduce the information and learning costs that they entail for cross border creditors. .

Both general objectives reinforce each other. The more efficient the insolvency regimes at national level, the more conducive they are to cross-border investment in the single market. The more similar the elements of insolvency rules are in Member States, the more active would be cross-border investors and therewith - the more intense would be competition among providers of funding and the lower would be the cost of financing for companies.

4.2. Specific objectives

The initiative aims to initiate a completion of the toolbox used in insolvency cases by adding specific, targeted elements to insolvency regimes, pursuing the following specific objectives:

- The development of more efficient and similar rules in Member States for better value recovery, notably in the fields of transaction avoidance, asset tracing, directors' duties and pre-pack procedures.
- The development of more similar rules in Member States for more efficient insolvency proceedings, notably with respect to MSEs procedures, insolvency triggers and insolvency rule transparency to support a timelier conclusion of insolvency proceedings for non-bank companies.
- The development of more similar rules for efficient and fair distribution of recovered values in Member States, notably in the field of creditor committees and the ranking of claims to reduce legal uncertainty and information costs related to insolvency processes for cross-border creditors.

Insolvency rules need to be consistent with the wider legal system in the Member States such as company law, labour law and property law. The convergence of insolvency rules should not compromise neither the consistency of national insolvency regimes with other parts of the national legal systems nor a fair treatment of debtors, creditors and other stakeholders in companies undergoing insolvency procedures.

5. WHAT ARE THE AVAILABLE POLICY OPTIONS?

The problem analysis identified a number of elements related to the value recovery tools, governance of proceedings, and tools for efficient value allocation typically used in insolvency cases that insolvency experts identified as either missing in national insolvency laws in some Member States or inadequate in other Member States to address the problems of overly lengthy and costly insolvency proceedings and low predictability of insolvency proceedings, notably for cross-border creditor. Building on those findings, this section assesses how the problem would evolve if there is no intervention (baseline scenario) and what policy options can be considered to address such problems. Annex 5 complements this section by providing more details on the individual building blocks.

5.1. What is the baseline from which options are assessed?

Without action at EU level, Member States are likely to either keep their existing insolvency regimes unchanged over the next years or introduce limited changes that would very likely not be aligned across the EU. After the transposition of the Directive on (preventive) Restructuring and Insolvency, which had to be concluded by July 2022, Member States are unlikely to enhance further the convergence between substantive elements of their national insolvency regimes.

Against the forecast of rising bankruptcy figures in light of winding down of public support measures related to Covid-19 and slowing economic activity as a consequence of the energy inflation shock,[129] a rising case load is likely to increase further the duration of insolvency proceedings. This could be partially mitigated by action by Member States to improve court capacity. Annex 6 reports on what kind of measures Member States already envisage to undertake in the area of insolvency in their reform and resilience plans. Furthermore, were not already done, Member States could also improve judicial capacity by making better use of digital means, as well as react to a rising number of insolvency cases by reallocating courts and judges' capacity to address bottlenecks. While such measures would partly help address the first identified problem, they are unlikely to happen in a uniform matter across the EU.

The prospect of a rising case load and widening divergence in the efficiency of insolvency procedures should be seen against the backdrop of a gradual improvement in cross-border investment flows stimulated by other CMU policy measures and the resulting more important role of cross-border creditors in this context. Increased cross-border activity is likely to exacerbate further the issue around the length and ensuing bottleneck of insolvency proceedings across Member States.

Ongoing (or future) CMU measures in other areas will not make this initiative superfluous, but should contribute to addressing other obstacles to cross-border investments.[130] In doing so, these proposals may also implicitly raise the potential number of cross-border insolvency cases in the future. The Commission proposal on the European Single Access Point for company data, once agreed by the co-legislators, should increase the visibility of companies across the EU and hence further facilitate cross-border investment.[131] The upcoming Commission proposal on the Listing Act should make the use of funding through public markets by companies more attractive, also contributing to more public offers of securities cross-border. Cross-border activity is likely to remain significantly below its potential if structural barriers, at least in the area of insolvency, remain unaddressed. The importance to tackle the insolvency-related barriers would remain irrespective of progress made on other determinants. Slow and costly treatment of cross-border creditors' claims in a liquidated estate and low value recovery, unless tackled, will serve as a serious obstacle and disincentive for them to engage in cross-border investment in the future, reducing the EU growth potential overall.

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[129] See for example, Demmou et al. (2021), Allianz Research (2022).

[130] IMF (2019) identified supervisory convergence and transparency of data as the other two important policy triggers to cross-border investment (in addition to national insolvency regimes). Other Commission initiatives aim at tackling these other areas (e.g. report on the operation of the European Supervisory Authorities and the proposal on the creation of the European Single Access Point).

[131] COM/2021/723 final, COM/2021/724 final and COM/2021/725 final.

The assessment of the quantitative impact of the envisaged policy measures will use, as a benchmark, the EU averages for recovery values, judicial costs and recovery time experienced by banks as creditors.[132] Since the numbers pre-date the COVID crisis, they are not distorted by the low bankruptcy numbers accomplished by the public support measures in the last years. They are the most recent indicators that represent "normal" business conditions and therefore considered to be suitable for the baseline. Although these values may not be necessarily representative of all creditors, variations in their values would be expected to closely mirror variations for other creditors.

5.2. Description of the policy options

Available policy options have been carefully selected and grouped, among others, considering the experience during the negotiatons of the Restructuring and Insolvency Directive, the deliberations and final recommendations of the expert group, the results from the public consultation, a study by an external consultant and extensive interactions with stakeholders. More specifically, the impact assessment considered the areas put forward for harmonisation of insolvency regimes by stakeholders in the public consultation. Furthermore, the group of experts on restructuring and insolvency law[133] elaborated on the scope of these areas. Finally, the external study (Deloitte and Grimaldi (2022)) provided further analysis on the impact of harmonisation in these areas and how the rules in question are currently applied in Member States.[134]

Measures that target different elements of insolvency proceedings are packaged in two options that differ in their degree of ambition. Option 1 focuses on targeted elements for which some commonalities already exist across Member States. They would not necessitate that Member States overhaul fundamental principles of their current national insolvency laws (and other areas of national law that are related to insolvency laws). Option 2 is more ambitious as it aims to address the problem more holistically. It includes some elements that certain respondents (e.g. corporates) to the public consultation signalled as obstacles to the efficiency of insolvency proceedings and the removal of which would be beneficial to foster cross-border integration. These in particular concern a trigger for insolvency proceedings and the ranking of claims.[135] As set out in later in this impact assessment (see in particular sections 7 and 8), the higher ambition in option 2 may, however, lead to potential conflicts with other areas of law in Member States, determined by differences in legal tradition, history and policy preferences across Member States.

The composition of those packages was intensely analysed, especially on the elements that distinguish the two options. The elements presented in option 1 reflect recommendations by insolvency experts about what they considered appropriate. Option 2 is a credible alternative to Option 1, reflecting the perspective of wider economic and business interests. Given the number of building blocks and links between them, the

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[132] Report on the benchmarking of national loan enforcement frameworks, EBA, 2020.

[133] https://ec.europa.eu/transparency/expert-groups-register/screen/expert-groups/consult?lang=en&groupID=3362

[134] See Deloitte/Grimaldi (2022).

[135] Although the ECB did not submit a response to the public consultation, the quote below indicates an important role for elements in option 2: "Market participants would find it easier to invest in firms located in different Member States if core elements of insolvency regimes, such as the definition of insolvency triggers, avoidance actions and the ranking of claims, were harmonised at best-practice levels", de Guindos et al. (2020).

present grouping of options was considered the only feasible approach to present options with different levels of ambition. Each option, by design, covers a number of elements to ensure that the reform under each option has a meaningful impact (which would not be the case if, instead of grouped options, each element would be presented as a separate option). No additional elements have been identified in interactions with stakeholders and experts, which would also be politically feasible and could thus be incorporated in either (or both) options.

Both options suggest legislative changes, namely through a new Directive, whereas the option to pursue them through a Recommendation was discarded from the onset (see section 5.3).

5.2.1. Option 1: Targeted measures on procedural efficiency and value maximization ('Targeted harmonisation')

Option 1 presents targeted measures grouped based on the problem driver they primarily address.

5.2.1.1. Measures targeting value recovery

Under this option, a set of targeted measures would aim to increase value recovery for all creditors, including cross-border creditors in the EU. More specifically, these measures would aim to increase the effectiveness of transaction avoidance rules and subsequent asset tracing for its recovery across the EU. Furthermore, they would aim to introduce more discipline on timely filing of insolvency to avoid unnecessary value destruction in case of delayed filings. Finally, they would seek to put in place harmonised rules on procedures allowing for better value recovery through a pre-pack arrangement.

In the case of transaction avoidance, a minimum set of harmonised conditions for exercising avoidance actions would be introduced. 84% of the respondents to the public consultation supported a more comprehensive harmonisation of avoidance actions and for the harmonisation of elements such as the different avoidance grounds, of the objective and subjective conditions leading to avoidance, as well as of the time periods prior to the opening of insolvency, which count as relevant for avoidance claims.[136] More concretely, the following key elements of the transaction avoidance legal framework would be clarified in EU law: types of suspicious transactions, avoidance grounds, related parties, the period during which the avoidance measures can be enacted, and, finally, legal consequences of avoidance, including the liability of third parties and rights of the opponent.

Transaction avoidance measures would be complemented by measures strengthening asset traceability through a better-facilitated access by insolvency practitioners to asset registers, notably in a cross-border setting (i.e. when assets have been moved to/acquired in another Member State during the period relevant for transaction avoidance rules). In the public consultation, almost 85% of the stakeholders favoured harmonised rules on assistance (including the interconnectivity of relevant registers) in the cross-border

[136] All stakeholder groups showed support for all of the proposed subjective criteria to be used as possible conditions to qualify a transaction as avoidable action. Also, the use of objective criteria was supported. The most often quoted objective criteria were that: 1) The transaction happened within the 'suspect period' (77%); 2) the transaction is to the detriment of the general body of creditors (70%); and 3) the debtor was insolvent at the time of the transaction (53%). The majority of stakeholders (74%) agreed that the 'suspect period' should be harmonized at EU level.

tracing of assets of the insolvent debtor. This would be achieved by enhancing in EU law the access rights of practitioners to a registry in another Member State. This can also build on the already existing arrangements for access to EU-wide interconnected registries (BRIS, BORIS, etc.[137]).

Furthermore, to avoid potential asset value losses due to a delay in filing for opening the insolvency proceeding, directors would be obliged to timely file for insolvency within a pre-defined period of time (e.g., at least within the three months of failing the insolvency test of the Member State). Directors failing to comply with this obligation would be held liable. The public consultation yielded widespread support (81%) for minimum harmonization at EU level of the duties and obligations of directors in the event of vicinity of insolvency or when the company is insolvent. In particular, the most beneficial aspect of harmonization would be to impose a duty on the director, once the company is insolvent, to file for insolvency proceedings (71%).[138]

Finally, under this option, a minimum set of harmonised standards for a pre-pack liquidation procedure would be introduced to maximise the value preservation in the sale of all or part of the business. The pre-pack rules would set out harmonised conditions for conducting negotiations on the sale of the business before insolvency filing, with the deal finalised in insolvency, hence enabling the realisation of the value of the insolvency estate right or shortly after the official opening of the proceedings. The pre-pack arrangement could thus avoid significant value destruction, which usually happens, when the assets can be realized only at a later stage of the proceedings, long after the opening.[139] The pre-pack rules would include safeguards to ensure transparency and equal treatment of creditors, to avoid abuses. In addition, these safeguards would need to ensure that employees' rights are not unduly curtailed by the pre-pack administration, including the right to information and consultation.

5.2.1.2.Measures targeting procedural efficiency

With SMEs being the backbone of the EU economy, it is important to ensure that the new rules work well also for smaller companies in the EU, for whom the cost of the ordinary (i.e. established) insolvency procedure is prohibitively high, and where a more rapid debt discharge would allow to unblock the entrepreneurship capital for new projects. Under this option, a special harmonised insolvency procedure would be set out in EU law tailored to the needs of micro and small enterprises (MSE). This MSE insolvency proceeding would be designed proportionally to the needs of MSEs, their creditors and other stakeholders, allowing them to be wound down orderly at low costs. Instead of establishing derogations for MSEs from the existing general rules of insolvency proceedings, this option would suggest a bespoke MSE procedure at EU level.

This specific procedure should follow a flexible, modular approach, in which the default liquidation process is run with reduced formalities and without the involvement of lawyers or insolvency practitioners. Additional elements, such as the involvement of an

[137] In its proposal for the 6th Anti-money Laundering Directive, the Commission proposed the EU-wide interconnection of the national centralized bank account registries. The proposal is being negotiated by the EU legislator. See COM/2021/423 final.

[138] Two thirds of the respondents supported a clarification that in the vicinity of insolvency directors should formulate plans to take preventive action.

[139] A functioning market for distressed assets would leverage the benefits of pre-pack sales.

insolvency practitioners or the ordering of a moratorium could be included optionally, on the request of the debtor or creditors, thereby keeping costs as low as possible. The procedure would set out simple rules on the entry conditions and the administration of procedures (including digitalisation and automation of key procedural steps[140] and the use of electronic auctions to generate revenues from MSE assets[141]). In order to make this procedure attractive for MSEs, the procedure would be coupled automatically with a debt-discharge. The system shall ensure that liquidations could also be carried out where the debtor's assets do not cover the costs of the procedure.

In addition, under this option, Member States would be required to further enhance transparency of the key features of their respective insolvency rules, by making such information easily accessible to investors on a public website and in a pre-defined user-friendly format, with the e-Justice Portal as default option.[142] This would take the form of a brief factsheet document with standardised key information that would be essential for (potential) investors to make a "glance-through" assessment of the insolvency framework in a given Member State, in a comparable way. The factsheet would provide targeted information about relevant insolvency triggers. It would also contain information on the average duration of an insolvency proceeding in a given Member State. A requirement for Member States to raise awareness among the potential investors on these factsheets would be part of the option.

5.2.1.3.Measures targeting the distribution of recovered values

To ensure a distribution of recovered values that is perceived as fair and predictable, this option introduces requirements for improving the representation of interest of the creditors throughout the proceedings and for enhancing the transparency about the ranking of claims.

In relation to the representation of the creditors in the insolvency proceedings the option would set out the minimum harmonisation requirements on creditors' committees. These measures would encompass the establishment of the committee, the organisation of meetings, the voting rules and the powers and duties of the creditors' committees.

As regards the ranking of claims of different types of creditors, the option would introduce enhanced transparency requirements to ensure that Member States make public the easily readable information on the ranking of claims in their jurisdiction in a simplified (user-friendly) format, possibly on the e-Justice portal. This disclosure should include references to national laws setting the ranking and possible exceptions to the standard ranking of claims in corporate insolvency.

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[140] Electronic communication with courts and IPs is standard in about 75% of the EU Member States. see Steffek (2019).

[141] The majority of Member States uses on-line judicial auctions, though few only in insolvency cases, see https://e-justice.europa.eu/content_judicial_auctions-473-en.do.

[142] While the e-Justice portal already includes some information on national insolvency proceedings, presented according to a Q&A template, the detail and presentation of information differs across Member States, making it difficult to consult especially for non-lawyers. Furthermore, while the Insolvency Regulation, which has introduced a requirement for Member States to include a description of national insolvency laws on the e-Justice portal, has been in application for several years, not all Member States have by now included the required information on the portal.

5.2.2. Option 2: A more comprehensive harmonisation of insolvency regimes in the EU ('Wide harmonisation')

Option 2, in addition to the policy options set out under option 1, would include a number of additional elements that would seek to pursue a more comprehensive harmonisation of national corporate insolvency rules across the three dimensions (value recovery, procedural efficiency and distribution of recovered values). This option is more holistic and ambitious, moving beyond what insolvency experts considered as broadly consistent with the existing rules in Member States and touching on the areas that are deeply intertwined not only with the fundamental principles of national insolvency laws, but also with other areas of law such as property, company or labour laws in many Member States.

5.2.2.1.Value recovery measures

On value recovery, option 2 would include the transaction avoidance and asset tracing measures, as well as the minimum standards on the pre-pack as set out under option 1.

In addition to those measures, option 2 would also include further reaching measures on asset seizure and recovery. Under this option, in addition to better equip insolvency practitioners to trace assets moved to another Member States, their ability to seize assets across borders would also be enhanced. A harmonised judicial mechanism could be set up in Member States' laws by the help of which insolvency practitioners of other Member States could easily freeze bank accounts or seize other assets belonging to the insolvency estate. Such a streamlined mechanism would complement the existing legal possibilities for insolvency practitioners, which – according to qualitative evidence – do not ensure asset preservation flawlessly.[143]

Furthermore, under option 2 a general principle would declare the shift of fiduciary duties of the directors of the company in the vicinity of insolvency. Hence, directors would be required to consider the interests of the creditors alongside the interest of shareholders. The requirements (and ensuing liability) would thus extend beyond a mere obligation to file for insolvency.

5.2.2.2.Measures targeting procedural efficiency

On procedural efficiencies, in addition to the special insolvency regime for MSE already set out under option 1, option 2 would also seek to harmonise the insolvency trigger (i.e. the start of insolvency proceedings) across Member States by putting forward a common liquidity criterion. This criterion would serve as the latest point in time by when the state of insolvency would have to be established. Member States would nevertheless be allowed to add a stricter (economic) test to bring forward the moment of the establishment of insolvency (but not to delay it). This harmonised liquidity test would set out the methodology for concluding on illiquidity of a company. It could for example set out that a company that was not in a position to meet its debt obligations within a pre-

[143] Under Article 21 of the EIR, insovlency practitoners have the same powers in other Member States as attributed to them by the law of the insovlecny proceedings (lex forum concursus), these powers have to be applied, however, in compliance with the law of the Member State within the territory of which it intends to take action. Insolvency practitioners may also resort to the rules of Regulation (EU) 655/2014 establishing a European Account Preservation Order procedure, but the scope of this instrument is limited.

defined period (e.g. 90 or 180 days) would be deemed insolvent. Court discretion and case-by-case assessment would be limited to exceptional cases.

Two thirds of the respondents to the public consultation supported a harmonised trigger for insolvency. The notable exception were the responses from public authorities. The most popular proposed common trigger for insolvency was based on a liquidity test.

5.2.2.3.Measures targeting distribution of recovered values

On distribution of recovered values, option 2 would, similarly to option 1, include the rules on creditors' committees. In addition to these rules, option 2 would also include a harmonisation of certain elements of the ranking of claims (without harmonising the full domain of ranking of claims that was deemed non-feasible and hence discarded upfront). Under this targeted harmonisation, rules would be introduced, for example, to exclude the privileged treatment of some unsecured claims, such as tax claims. The responses to the public consultation on the ranking of claims were met with certain opposition from at least some groups of stakeholders. Furthermore, there was overall opposition to the proposed harmonisation of the carve-out rules (i.e. when a group of creditors is given preferential treatment by being treated before any creditor in the ranking of creditors) and of rules to protect 'new-financing'

5.3. Options discarded at an early stage

This initiative focuses solely on traditional insolvency proceedings, to complement the existing minimum harmonisation on preventive restructuring. Elements in insolvency regimes that deal with preventive restructuring schemes, i.e. mechanisms that can be accessed by the debtor before the state of formal insolvency under national law, were, thus, discarded upfront from being part of any option.

Table 3: Measures under the two policy options

	Option 1 **Targeted measures on procedural efficiency and value maximization**	**Option 2** **A more comprehensive EU insolvency regime**
	A1: measures that target asset recovery:	
Transaction avoidance	Minimum harmonisation (i.e. stricter national rules permissible) of specific rules, such as scope of legal acts concerned, avoidance grounds, definition of related parties, the period before insolvency under scrutiny, legal consequences of avoidance /including the liability of third parties/ and rights of the opponent	As in option 1
Asset tracing and recovery	Improving access of IPs to asset registers abroad, with focus on access via systems of EU-wide interconnections – BRIS, BORIS, etc.	Enhancing the ability of IPs to seize assets in other Member States. Improving their access to asset registers abroad and their direct powers of seizing or recovering assets from abroad.
Directors' duties and liability	Obligation to file for insolvency (within a time limit no longer than 3 months) and related liability	In addition, a change of fiduciary duties of the directors in the vicinity of insolvency
Going concern sales in insolvency	Minimum standards for a pre-pack liquidation regime	As in option 1
	B1: measures that improve procedural efficiency	
Insolvency trigger	Obligation to enhance transparency (public [e-Justice Portal] website) of the main elements of insolvency rules, including insolvency trigger	Targeted harmonisation of liquidity criterion for the latest possible triggering of the procedure
Specific treatment of micro- and small enterprises	Special liquidation procedure for MSEs coupled with a debt discharge for entrepreneurs (this should be an expedited, low-cost procedure, that also applies in asset-less scenarios).	As in option 1
	C1: measures that govern the distribution of recovered values:	
Ranking of claims	Obligation to enhance transparency (public [e-Justice Portal] website) on creditor ranking	Harmonisation of the treatment of public claims
Creditors' committees	Minimum standards (i.e. rules at national level providing more influence for creditors are permissible) on the elements of establishment, meetings, voting rules, powers and duties of creditors' committees. Setting up a committee in individual cases would depend on the decision of the creditors.	As in option 1

The analysis in preparation of this impact assessment revealed that Member States' starting positions on the harmonisation of ranking of claims are very different and are strongly linked with other national policy objectives, values and legal traditions (such as the protection of employees). Moreover, their interference with other parts of legal systems imply that harmonisation in this area is likely to affect in a significant manner in particular national property and labour laws. The option to introduce a comprehensive harmonisation of the ranking of claims was therefore discarded as potentially problematic from subsidiarity perspective and politically non-feasible.

The option to propose non-legislative measures was also considered at an earlier stage. The public authorities that replied to the public consultation expressed a strong preference for a recommendation, the insolvency practitioners for a combination of a legislative instrument and a recommendation, whereas all other participants (including corporates) favoured a legislative instrument (either on a stand-alone basis or in combination with a recommendation). Following an assessment, it was concluded, however, that non-binding measures, such as a Commission Recommendation, would be insufficient to entice Member States to conduct sufficient reforms in the complex area of insolvency. Non-binding measures are highly unlikely to be sufficient to ensure the harmonisation of insolvency regimes that are at present very different across Member States. This is corroborated by recent experience in the area of EU insolvency policy. The invitation addressed to Member States in the form of the Commission Recommendation of 12 March 2014 on a new approach to business failure and insolvency (2014/135/EU) was only sporadically followed by them. Even those who enacted national legislation on the basis of the Recommendation, have done this in a divergent and inconsistent manner, that did not produce convergence towards the standards suggested in the Recommendation. It has therefore been deemed subsequently necessary to propose the Restructuring Directive.[144]

Given the proximity of the policy areas covered and the general sensitivity of the matters related to insolvency law, a similar outcome could be expected for non-legislative measures in the context of this initiative so that it seems justified to discard that as an option. Therefore, the impacts of a non-legislative measure that would contain the same elements as those set out in options 1 or 2 are not assessed in this impact assessment. Based on the recent experience referred to above one would have to expect a very limited uptake and, even in the event of an uptake, it would have to be expected to be uneven across those Member States that would take measures. Any impact from a recommendation would thus be at best a small fraction of the impacts identified under either of the two options, with the analysis highly conditional on (likely to be random and hence speculative) assumptions about the level of voluntary uptake in Member States.

6. WHAT ARE THE IMPACTS OF THE POLICY OPTIONS?

The initiative will improve tools in all Member States to create the conditions that could reduce the duration of the proceedings or recover more value. Whether this potential will be exploited will depend on the application in practice. It will for example depend on whether the judicial system has the capacity to deal with insolvency cases and IPs have

[144] OJ L 74, 14.3.2014, p. 65–70. Similarly, a self-regulation instrument, such as the aforementioned UNCITRAL Legislative Guide, is difficult to apply in the area of substantive insolvency laws, where there is a strict legislative regulation in all Member States, which is highly divergent from one Member State to the other.

no incentive to abuse the additional powers they would be entrusted with. The analysis of the impacts assumes that the two factors outside the scope of the initiative, i.e. the organisation of courts and the regulation of IPs, do not act as deterrent to the effective use of the enhanced tools at their disposal. Judicial capacity is likely to become an issue if the expectation of a higher number of corporate insolvency cases materialises. Most of the measures discussed in this impact assessment, however, are expected to lead to shorter procedures and lower judicial costs, with the exception of the MSE regime, for which the countervailing effects are further discussed in more detail below.

6.1. Benefits and costs of a targeted regime

6.1.1. Measures targeting asset recovery

Targeted measures in this area would increase the value that can be recovered from the liquidated estate, with the largest benefits expected in those Member States that have not yet implemented efficient practices in this area. In those Member States, insolvency practitioners, whose task it is to preserve the insolvency estate in the collective interest of the creditors, would be equipped with better tools to preserve value. More efficient rules would allow and encourage insolvency practitioners to focus on avoidance actions early in the administration, avoiding procrastination in ascertaining whether certain transactions may be revoked. Moreover, they would enable insolvency practitioners to collect the necessary evidence and be sufficiently meticulous in their investigation.[145] Almost 84% of the stakeholders in the public consultation favoured harmonised rules on assistance (including the interconnectivity of relevant registers) in the cross-border tracing of assets of the insolvent debtor.[146] In particular insolvency practitioners and researchers supported EU action in this area, whereas the support of public authorities, financial and non-financial business entities was somewhat less pronounced. Almost 90% of the stakeholders agreed that insolvency practitioners should have full access to property and collateral databases.

The possibility to use pre-packs in all Member States that do not permit this tool yet would improve the recovery value and could shorten the duration of insolvency cases in those Member States. The requirement for directors to file timely and the associated liability for them would further limit value destruction in the vicinity of insolvency. The public consultation revealed widespread support among stakeholders (81%) for minimum harmonisation at EU level of the directors' duties in the vicinity of insolvency or when the company is insolvent.[147] Nevertheles, the extent of support varied depending on a stakeholders' group. Whereas 93% of the practitioners/professionals supported minimum harmonization at EU level of the directors' duties in the vicinity of insolvency, only 50% of the public authorities were of the same opinion.[148]

More efficient rules on transaction avoidance – as supported by 84% of the respondents to the public consultation - would be beneficial for all *creditors*, whether they are

[145] See Keay (2018).

[146] Stakeholders' replies to the more detailed questions reveal that such rules would be most useful in relation to the following types of assets: real estate (78%), company interest (60%), bank accounts (75%) and claims other than those arising from bank accounts (46%).

[147] In particular, the most beneficial aspect of harmonisation would be to impose a duty on the director, once the company is insolvent, to file for insolvency proceedings (71%).

[148] With an average rating of 2.8 assigned by insolvency practitioners/lawyers and 1.5 by the public sector on a 0 to 5 scale (see Figure 8).

domestic or cross-border. Nevertheless, given their inherent information disadvantage and resulting increased difficulties to influence the running of the proceeding, cross-border creditors would stand to benefit even more than domestic creditors if the rules on avoidance actions become more similar, efficient and transparent. Stakeholders signalled that the enforcement of in particular cross-border assets and the detailed and divergent rules applied across Member States have led to differences in the amount that could be recovered and the time it could take to claw back assets. Hence, more harmonised rules on transaction avoidance and asset tracing would help to level the playing field and to increase value recovery, notably in cross-border proceedings. Enhanced possibilities, through a more facilitated access to asset registries in other Member States to trace assets abroad, would also reduce the costs for *insolvency practitioners* (and insolvency proceedings overall).

For *cross-border creditors*, transparency and alignment of rules are particularly important.[149] For example, while cross-border creditors would benefit from the possibility to opt for a pre-pack procedure – another tool enhancing value recovery – they may see themselves disadvantaged if the rules governing the pre-pack are opaque and accountability is unclear. Only subject to the necessary safeguards for the protection of interests of all affected creditors in pre-packs, the measures would make it overall less costly for cross-border creditors, including by making it easier for them to find out about the respective rules in other jurisdictions and to assess the prospects for claw-back. Creditors from third countries face the same challenge as cross-border creditors within the EU.

Furthermore, *creditors* stand to benefit from improved tools for value recovery not only in insolvency, but also long before it – notably when making their decision to invest. Since the more efficient and aligned rules around value recovery increase creditors' confidence to obtain better or fairer access to the debtor's assets in case of insolvency, they allow for more certainty in assessing the cost of capital against which credit is granted. In particular, when rules are more aligned across Member States, creditors who give a loan to a debtor in another Member State will find it easier to evaluate the impact of transaction avoidance law of another Member State (compared to their own) in their assessment of the consequence of the debtor's insolvency on their investment[150].

The conduct of the *insolvent companies and their directors* is key to influence the prospects of value maximization and recovery rate in the concrete proceedings. The introduction of more efficient rules on directors' duties and liabilities would address the moral hazard problem and reinforce the incentive to timely file for insolvency (as a counterweight to the aversion to acknowledge business failure), which is likely to increase the recovery value. Company directors would face higher liability risks, which may lead them to demand higher salaries, and likely higher premia for liability insurance. While honest debtors would not undertake measures to procrastinate the filing of insolvency, hide assets or divert them at the brink of insolvency, such opportunistic

[149] While not a subject of the public consultation, the survey by Deloitte and Grimaldi (2022) revealed that about 80% of the interviewed insolvency experts supported measures towards more transparency. See Table 4.

[150] The applicable law in question is that of the *lex fori concursus* (Art. 7(2)(m) EIR), which can be mitigated for the interest of the creditor by a more lenient rule of the *lex causae* (Art. 16 EIR). Both laws can be different than the law of the State where the creditor resides.

behaviour at the expense of creditors has been observed in practice.[151] The new measures would discourage and limit the ability of those debtors to hide assets.

The impact of changes in these areas on the *public sector* is expected to be small. Nevertheless, they can lead to lower incurred costs of judicial review if procedures become shorter. It is also possible that easier cross-border asset tracing and seizure leads to higher demand for court involvement. While it is not possible to provide numerical estimates to what extent this latter effect could impair judicial capacity, the analysis in Annex 4 suggests for which Member States judicial bottlenecks are more likely to be an issue (see also section 6.1.2). They are hence the ones more likely to (but not necessarily) be exposed to any possible adjustment costs (if such costs materialise) from the introduction of the proposed measures, leading to potential procedural delays. Since option 1 is calibrated to target only those elements in insolvency regimes where the harmonised rules do not introduce major inconsistencies with other pieces of national law, the impact in terms of the need to provide additional legal clarity or adjust other pieces of national law should be limited. Exceptions could stem from the need to address possible issues from avoidance actions on property rights and from asset tracing on data protection.

6.1.2. Procedural efficiency measures

In the presence of transparency about the key features of insolvency regimes, both *creditors* and *debtors* would be able to assess under which conditions an insolvency process starts and how it will run its course. It means procedures related to the beginning of protective measures (e.g. avoidance actions), beginning of insolvency proceedings (e.g. insolvency trigger), use of outside expertise (e.g. insolvency practitioners), governance supporting effective decision making (e.g. creditors committee). This allows *debtors* to react effectively (and if necessary pre-emptively) as well as for *creditors* to seek solutions. These measures towards procedural efficiency would allow to shorten proceedings at certain, more difficult phases, allowing for quicker and fairer decision making and for more efficient running of proceedings overall.

Transparency on insolvency triggers reduces uncertainty to *creditors* and in particular to cross-border creditors, who would incur lower information and learning costs. This should translate into a higher willingness of these investors to provide credit to companies at the beginning and lower cost of financing to those companies as a result. The Deloitte/Grimaldi (2022) study reports that insolvency experts attribute sizeable efficiency gains to more transparency in a cross-border context, supporting the notion that information costs are an important obstacle in practice (see Table 4).

In addition to better transparency, which would empower both *creditors* and *debtors* to use the most effective toolkit to ensure a more efficient proceeding, procedural rules could also be made more proportionate to a specific type of a company in insolvency. Thus, a dedicated MSE liquidation procedure, by reducing formalities, increasing the use of electronic means of communication and limiting the involvement of insolvency practitioners and lawyers would reduce the costs of the procedure. Together with the statutory debt-discharge, this would make the insolvency regime more attractive for ailing debtors (entrepreneurs). Better access to insolvency procedures would reduce the debtors' (i.e. entrepreneurs') bias towards keeping the company alive as long as possible.

[151] See the insolvency case of a drugstore chain in Germany 2012.

The conduct of insolvency proceedings even in cases where today such proceedings are not opened because the assets of the debtor do not cover the judiciary costs (so called 'asset-less cases'), would generate additional costs for financing these proceedings (possibly for the *public budget*, the *businesses* or *insolvency practitioners*). These additional costs as well as the costs of dealing with a higher overall number of insolvency proceedings[152] are, nevertheless moderate as this simplified procedure would entail much lower costs than those of normal insolvency proceedings. The cost also needs to be considered against the potentially sizeable benefits of orderly winding down of distressed micro- and small businesses, coupled with a debt-discharge for the entrepreneurs concerned. Since the bankruptcy of a MSE has direct consequences for the entrepreneur, a fast and orderly liquidation through MSE procedures could accelerate discharge and help create a second chance for these entrepreneurs.

In general, *cross-border creditors* tend to be less exposed to MSEs given their low transaction value (also known as 'investment ticket size') compared to larger companies. However, once can observe that cross-border creditors started to take interest, for example, in very innovative start-ups that are prepared to pay high-risk premia for access to capital. In those cases, cross-border creditors would favour a possibility for a quick, efficient and low-cost winding down of a company.[153] Furthermore, with other policy measures ongoing at EU level to increase the visibility of SMEs across Member States (such as the creation of the European Single Access Point for company data[154]), the number of cross-border creditors taking interest in SMEs is likely to increase in the future. Since the proposal seeks to ensure a quicker value recovery in MSEs, it makes MSEs more attractive for cross-border investors, complementing other actions under the CMU. An investor association indicated that risk-capital investors (e.g., private equity firms) see virtue in second chances and hence a quick debt discharge for innovative and driven entrepreneurs. For *smaller creditors* of MSEs (which are likely to be in majority for MSEs), ill-placed to absorb high fees of insolvency practitioners, the MSE regime would also help reduce legal costs.

The fact that national insolvency frameworks are not always adapted to treating properly (and in a proportionate manner) insolvent MSEs represents a lost opportunity for the economy: these companies are in many cases deprived of the possibility to benefit from an orderly exit (if unviable) or from an adequate restructuring (if viable). This would apply to a very large number of EU companies, given that MSEs represent in some Member States up to 90% of the total count and 98% of the firms that exit.[155] The entrepreneurship capital becomes effectively locked in these companies, which become in many cases zombie-companies, with founding entrepreneurs unable to benefit from debt discharge in a timely manner and unable to start anew sufficiently quickly. Establishing a more proportionate regime for MSEs, and in particular granting access rights for MSEs to insolvency proceedings, would mean that more EU micro companies

[152] As a consequence of the fact that companies who, at present, are not eligible for insolvency proceedings or are not interested in going under the protection of insolvency, due to the high costs, will opt for the expedited procedure

[153] For a case study on cross-border transfers of SMEs, see European Commission 'Improving the evidence base on transfer of business in Europe: annex C: case study on the cross-border dimension of business transfers,' February 2021, available at: https://data.europa.eu/doi/10.2826/94014.

[154] Proposal for a Directive of the European Parliament and the Council amending certain Directives as regards the establishment and functioning of the European single access point, COM(2021) 724 final.

[155] 94.3% of enterprises in the business economies had 0 to 9 employees in 2018 according to Eurostat numbers for the EU-27 and would be counted as MSEs.

would be liquidated in a court insolvency proceeding (rather than outside one, which is often the case today).

Numerical estimates of the impact of this option on the length of proceedings and the outcome of the insolvency process are difficult to get by because by their nature, there is no good basis to estimate the level of information and learning costs. However, the insolvency practitioners surveyed by Deloitte Grimaldi (2022) point to a reduction in recovery time and an increase of the recovery value of about 12% if a harmonised MSE regime is introduced. They reported sizeable efficiency gains from the introduction of tools that provide transparency about insolvency triggers and other features of insolvency regimes, suggesting that the benefits could be sizeable.

Table 4. Indications from insolvency experts about the impact of harmonisation on the cost and time of insolvency procedures as a result of EU rules in the different areas.

	MSEs regime		Transparency	
			Glossary*	Standard ontologies**
	Cost savings	Time savings	Increase in efficiency	
Approval rate+	52.5%	52.6%	87.5%	77.4
Amount in %	11.9	12.5	NA	NA
Efficiency score ***	0.6		1.1	0.9

*Note: + share of the interviewed 120 insolvency experts that indicates the measure would lead to a decline in costs or time. % values are calculated as weighted average of the mean of the ranges indicates. They show by how much % the average insolvency expert thinks costs or time would decline. See Annex 4 for full numbers and more details. * A glossary of insolvency terms and of the equivalent professional figures in different jurisdictions, **A set of concepts and categories in the insolvency subject area and domain showing their properties and the relations between them, *** 0 indicates no efficiency gains, 0.5 marginal gains, 1 gains and 2 significant gains and likewise for negative values.*

Source: FISMA with Survey data from Deloitte/Grimaldi 2022.

The public sector could benefit from a simplified MSE insolvency regime because it reduces the costs of judicial review. MSEs that already have insolvency proceedings opened (or will open them in the future) before the court under the ordinary procedure would switch to a more alleviated and quicker one, economising judicial capacity. For example, the introduction of an MSE regime in France in 2019 aimed to reduce the time of judicial review from more than two years to one; cost savings could be proportional to the expected time shortening. Member States may also realise cost savings by using their existing electronic auction platforms for seized assets to sell assets of insolvent estates to foster quick and cost-efficient realisation of proceeds. The creation of cross-border links between these auction platforms would enlarge the potential bidder base and therewith on the proceeds that can be realised. The new regime may also allow for a possibility for MSEs to have a full debt discharge in an out-of-court setting, e.g. before competent administrative authorities, with faster and cheaper procedures.

Furthermore, the introduction of a simplified regime for MSEs will not necessarily lead to a higher number of insolvency cases by micro enterprises across all Member States. For example, it has not been observed in France since 2019, following its introduction.[156] It is, however, likely to increase the case load in those Member States that practice to reject applications for opening insolvency proceedings because of a lack of assets in the insolvent estate. Deloitte/Grimaldi (2022) reported that some "Member States do not even open (i.e. Austria, Germany, Greece and Italy) or immediately terminate

[156] The estimates in Annex 4, Section 4.1 show a negative correlation between business exits and the recovery rate, suggesting that there may be fewer business exits in a more efficient insolvency regime.

proceedings (i.e. Belgium and Spain) if the debtor does not have sufficient resources to cover at least the proceedings' expenses." In Germany and Austria, it applies to about 30% of the cases.[157]

Annex 3 provides some numerical estimates about the potential effect of the introduction of an MSE regime on judicial capacity under the assumption of a proportional increase in the case load for judges and no cost savings from other measures. The scenario analysis suggests judicial costs could vary between EUR 900 million up to a maximum of EUR 2 billion. The underlying calculations and assumptions are further detailed in Annex 4, Section 3.2. Nevertheless, key assumptions underlying these calculations are highly uncertain. Some aspects of the impact on the judicial capacity remain to be impossible to quanify.

The calculations do not incorporate two mitigating effects of the MSE regime that should reduce costs for the public sector. First, even when insolvency proceedings are not opened for MSEs due to a lack of sufficient assets, a judge still has to establish that the conditions of opening are not met and take the decision to refuse the opening of insolvency proceedings. These steps generate judicial costs, although they usually are lower than those of opening and conducting a full-fledged insolvency proceeding. Second, the opening of insolvency proceedings concentrates the handling of all claims against the debtor in the insolvency proceedings and makes it therefore inadmissible for creditors to enforce their claims through individual enforcement actions. If insolvency proceedings are not opened, individual creditors can and often go to court anyway to get a judgment that in reality may only become enforceable when the MSE has assets again. Courts therefore often have to deal with multiple proceedings on claims by creditors against the insolvent business, negatively impacting the available judicial capacity in a Member State. These effects are likely to mitigate significantly or even outweigh completely the additional costs (i.e. a possible negative impact on judicial capacity) from the new MSE regime. Finally, even in case the introduction of the MSE regime increases (which is not certain) costs for the *public sector* due to the impact on judicial capacity,[158] it will have a positive impact on the *economy and growth* overall due to earlier discharge of failed debtors.

Annex 4, Section 3.2 attempts to identify which Member States' judicial capacity could be particularly vulnerable to a higher caseload. The assessment uses two metrics of judicial efficiency – clearance rates and time of non-criminal court cases[159]. It is assumed that Member States with a currently already low clearance rate and longer duration of insolvency cases are likely to experience even more difficulties in coping with the consequences of introducing the MSE regime, notably if the latter leads to more insolvency cases to be brought before courts. Based on these metrics, Cyprus, Ireland, Spain and Malta were identified as the Member States that would potentially be the most exposed to a possible negative consequence from the MSE regime on their respective court capacity. Spain has, however, just introduced a special shortened insolvency procedure for micro-companies with a value of less than two million euros or with fewer

[157] See Annex 4, Section 3.2.

[158] The costs of an MSE regime depend on the number of MSEs that use an insolvency procedure relative to those that are closed without an insolvency procedure. The costs to the public sector also depend on the share of assetless MSEs that use an insolvency procedure, see Annex 4, Section 3 for assumptions and estimates of quantitative effects.

[159] The indicators were taken from CEPEJ (2022), which is underlying the EC Justice Scoreboard.

than ten employees. Since this procedure is already available also for microcompanies with no assets, the EU MSE regime is unlikely to lead to a further significant impact (beyond that from the implementation of the national regime) on its judicial capacity.

In addition to the costs for the *public sector* from a possible increase in insolvency proceedings, the public sector would also incur limited additional costs from developing the tools for better transparency on the features of insolvency regimes and insolvency triggers.[160] Since the basis for such tools is already available on the e-justice platform, it should be possible to achieve it without considerable additional investments. It is estimated that the development of factsheets for better transparency in all EU Member States may cost from EUR 67 000 to EUR 90 000.[161] These costs are mainly of a one-off nature and are likely to be by far outweighed by reducing the economic cost of legal uncertainty, such as a lower (than could otherwise be) level of cross-border investment and the need to procure expensive legal advice in the vicinity of insolvency.

6.1.3. Measures targeting the distribution of recovered values

Well-defined rules about the role of creditor committees and transparency about the ranking of claims would reduce the costs associated with deciding on how the recovery value should be distributed among the creditors. They may have little impact on the role of debtors. Nevertheless, as these rules could reduce the costs of negotiations with creditors, both the *debtor* and the *insolvency practitioner* tasked with the liquidation of a company would be expected to see their costs reduced.

Creditor committees allow *creditors* to cooperate and more effectively coordinate their decisions, which is important given that multi-creditor lending relationships are common in the EU. Creditors may have different views about the best way forward, face collective action problems and can generate holdout problems that may prevent the insolvency practitioners from achieving an agreement that maximises the collective interest of all creditors. Clear rules on the role of creditor committees reduce the time and costs to find common solutions, which reduces the risk of holdout problems and may increase the recovery value. The survey by Deloitte/Grimaldi (2022) asked insolvency experts whether EU rules on creditor committees could yield time savings: almost two thirds of those who voiced a view on this agreed. According to the respondents, the presumed reduction in time thanks to creditor committees could amount to 1.4%.

While creditor committees ensure that the common interest of creditors is adequately protected, representation in creditor committees is more costly for *cross-border creditors* and their bargaining with other creditors is more complicated. Hence, similar (i.e. more aligned) and efficient rules on key aspects of powers and roles in creditors' committee can help especially cross-border creditors to exercise their rights and lead to a fairer treatment, thereby making cross-border lending more attractive and further reducing the cost of capital for companies.

More transparency on insolvency rules partly compensates for the difficulties for *cross-border creditors* arising from language barriers, translation obligations and from being less familiar with the position of other creditors. Especially the complexity of the national insolvency rules pertaining to the ranking of claims may make the outcome

[160] The provision of transparency on insolvency regime has the character of a public good. The non-rivalry of information leads to a suboptimal degree of transparency when organised by private actors.
[161] See Annex 3.

particularly difficult to anticipate for cross-border creditors. Transparency about the ranking of claims means investors are better able to assess what part of the residual value of the company will be distributed to them.

When a company is wound down, employees, tax authorities and other public authorities including those administering the procedure often enjoy preferential treatment that puts them above other creditors. Transparency on creditor ranking and common rules on the role and powers of creditor committees would reduce tensions in the actual negotiations with other creditors, while leaving the choice about the actual ranking to the Member States. They are likely to lead to less disputes about the decisions of insolvency practitioners and fewer reviews by courts of their decisions, which would be to the benefit of both length and costs of insolvency proceedings for the *public sector*.

The role given to creditors' committees in an insolvency regime is directly linked with the roles attributed to other actors (courts, insolvency practitioners) – and altogether these rules ensure the appropriate balance between the interests of creditors and debtors. Common rules on creditors' committees may therefore require the public sector to ensure consistency with other laws governing property rights. This would lead to some adjustment costs for the public sector.

Table 5 summarises key benefits and costs for the different stakeholders involved.

Table 5. Key benefits and costs, by stakeholder type – Option 1 (see also Annex 3)

	Creditors	**Cross-border creditors/ investors**	**Insolvent company and directors (going concern)**	**SMEs**	**Employees**	**Insolvency practitioners**	**Public sector**
Benefits	- Less assets being diverted from the insolvency estate (indirect) - Less costs for the lodging of claims and participation to the insolvency proceedings (direct) - Value maximization of distributable assets through more effective tools (asset recovery, directors' duties, pre-packs, direct) - Better coordination among creditors to maximise value recovery and efficient distribution (creditors committees, direct)	- Similar to domestic creditors - Lower information and learning costs (costs of familiarizing themselves with the rules of the foreign regimes) through greater transparency and comparable factsheets (direct). - Easier participation and greater influence in proceedings through standardized rules on creditors' committees (direct)	- More certainty about when the company is insolvent (direct) - Higher chances of timely selling going concern parts of its business (indirect)	- Increased availability of an orderly liquidation for micro- and small businesses in financial distress - Debt discharge for entrepreneurs concerned by the liquidation of MSEs (automatic second chance) - Access to orderly liquidation in asset-less cases reduces MSEs moral hazard (indirect)	- Higher chances to preserve employment for going concerns parts of the business (indirect)	- Easier access to asset tracing registries (direct) tools to recover value from asset disposal (e.g. avoidance actions; direct)	- Shorter insolvency proceedings overall (indirect) and for MSEs specifically (direct)
Costs	- In prepacks limited options for involvement in negotiations compared to standard restructuring	- Familiarisation costs (likely small or negligible)	- Higher liability of directors may be reflected in higher wage demands, more difficult recruitment of directors, company procedures / information flows or higher liability insurance costs (indirect) - Further internal procedures and an information flows to enable due diligence in case of a pre-pack sale (indirect) - Familiarisation costs (likely small or negligible)	- Higher liability risks for directors and entrepreneurs (indirect) - Familiarisation costs (likely small or negligible)	- Negligible	- Increased costs if MS decided to finance the treatment of asset-less cases through IPs	More proceedings for assetless MSEs (indirect), costs to establish and maintain transparency tools (direct)

6.2. Benefits and costs of a comprehensive EU regime

6.2.1. Measures targeting asset recovery

Option 2 foresees a wider harmonisation of the asset recovery measures, beyond the elements targeted in option 1 (transaction avoidance, asset tracing and directors duties) than the targeted measures.

More specifically, in comparison to option 1, option 2 includes two additional ambitious elements, which would allow for a more far-reaching insolvency reform at EU level: directors' duties and options for IPs to seize assets abroad. If directors are under the obligation to consider the interests of the creditors alongside the interest of shareholders (and may be held liable if they fail to do so), they face an incentive to take less risks in their business decisions to avoid insolvency becoming a possibilility and initiate proceedings earlier than without such liability. Whether this stronger incentive leads to material changes in directors' behaviour will depend on specific circumstances and is likely to be different across companies and directors. It will also depend on the courts' capacity to ensure effective enforcement. If creditors consider their interests better protected uniformly across the EU, they would face lower transaction costs when considering credit to entities in other Member States. The flip side of stronger liability vis-à-vis creditors in the vicinity of insolvency are potential loyalty conflicts between shareholders and directors that shareholders need to consider when appointing directors.

Better opportunities for insolvency practitioners to seize assets would facilitate their work, speed up the recovery process and are likely to increase recovery values. Since they currently face hurdles to act in cross-border insolvency cases, their empowerment to asset seizures could significantly improve their efficiency. The stronger powers for insolvency practitioners could also reduce the likelihood that transaction-avoidance actions are carried out in the run-up to insolvency. Creditors would benefit from this action, especially when engaged in credit to cross-border companies. Honest debtors should not be negatively affected by these rules.

Overall, both these elements are likely to lead to a higher value recovery for investors, including cross-border creditors, in the EU. Deloitte/Grimaldi (2022) interviewed insolvency experts about their expectations regarding how an EU regime on the different elements would impact on the costs of recovery and the time of insolvency procedures. A large majority of the 120 respondent expects savings of cost and time from the comprehensive harmonisation of the different elements. Their numerical estimates suggest a significant improvement in the range 9-16%.

Table 6: Indications from insolvency experts about the impact of comprehensive harmonisation on the cost and time of insolvency procedures as a result of EU rules in the different areas

	Avoidance actions	Asset tracing	Directors duties	Prepacks
Cost Savings				
Approval rate+	57.4%	60.0%	47.5%	58.3%
Amount in %	10.0	13.4	9.3	13.5
Time savings				
Approval rate+	54.1%	65.1%	46.7%	67.5%
Time of procedures in %	16.1	16.1	9.4	12.6

Note: + Share of the interviewed 120 insolvency experts that indicated the measure would lead to a decline in costs or time. % values are calculated as weighted average of the mean of the ranges indicates. They show by how much % the average insolvency expert thinks costs or time would decline. See Annex 4 for full numbers and more details.
Source: FISMA with Survey data from Deloitte/Grimaldi 2022.

However, at the same time, both elements are also likely to be much more difficult to fit into the existing legal orders of the Member States, potentially causing frictions with other areas of national law. For example, the redirection of directors' duties from shareholders to creditors would conflict with the existing provisions in company law in Member States. Addressing these issues would lead to follow-on costs for the *public sector* because it would need to restore the consistency with these parts of national law. Furthermore, it is likely to lead to certain legal uncertainty, at least at the beginning (until the relevant aspects of national law are fully clarified and jurisprudence of the court is settled), and adjustment costs in companies if shareholders want to appoint different directors in anticipation of possible loyalty conflicts. This would lead to costs for *companies* and *creditors* who would have to revert to expensive legal advice. The insolvency specialists in the expert group advised that these costs could be substantial and may thus outweigh the incurred cost savings.

Respondents to the public consultation were on average as supportive to a clarification that directors should secure the interest of creditors in the vicinity of insolvency as to the introduction of an obligation to file for insolvency.[162] They were less supportive to introducing minimum standards at EU level that lead to the establishment of liabilities for directors.[163] The public sector and the stakeholder groups that represent potential debtors and creditors, i.e. non-financial and financial business, expessed the most critical view on the establishment of liability for directors, whereas insolvency practitioners and researchers were most supportive of such a measure. Although the public consultation did not explicitly ask for views on asset seizure, stakeholders that replied to related questions expressed stronger support for the less intrusive powers for insolvency practitioners.[164] The public support for harmonisation in this area may therefore be limited. Responses from public authorities and non-financial corporates on the debtors' side were most critical, while those from research and financial corporations on the creditors' side were on averge more supportive of more intrusive measures.

6.2.2. Procedural measures

In addition to the improvements to procedural rules foreseen in option 1, option 2 would seek to align across the EU the test for the insolvency trigger. By establishing a point when the company can no longer procrastinate the start of the insolvency procedure, a liquidity trigger would bolster recovery values. A common test would ensure a timely insolvency start over the debtor's estate across the EU, removing differences across and inefficiencies in some Member States. In practice, it would harmonise the notion of insolvency that would introduce a harmonised reference point also for other elements of the insolvency regime, including for determining the scrutiny period for avoidance actions.[165]

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[162] Two thirds of the respondents supported "A clarification of the focus of duties of the director when a company is near to insolvency or is actually insolvent to look at the interests of the creditors". Two thirds also supported "A duty of the director, once the company is insolvent, to file for the appropriate insolvency proceedings".

[163] Half of the respondents supported this.

[164] More than two thirds of respondents supported powers to compel the production of books and records and to conduct audits compared to one third that supported search orders or the duty to report suspicious transactions to law enforcement authorities.

[165] It could also play a role outside insolvency procedures for example in state aid procedures that could benefit from a harmonised determination of firms in difficulties.

It follows from the broader scope that cross-border *creditors* would benefit more from a harmonised insolvency trigger than from the mere provision of transparency about the multitude of triggers across the EU Member States (foreseen under option 1). Since differences in insolvency triggers are sizeable at present, such harmonisation can generate sizeable savings for cross-border investment on information, learning and legal advice. Researchers and consultancy services supported overproportionally the harmonisation of insolvency triggers in the public consultation. Public authorities and stakeholders representing non-financial business were the least supportive.[166] Two thirds of respondents to the public consultation favoured a liquidity criterion.[167] The support was spread evenly across all stakeholder groups, except for respondents from the public sector, who favoured the combination of two triggers (a liquidity criterion complemented with a balance sheet criterion).

While a harmonised trigger reduces uncertainty to creditors and in particular to *cross-border creditors*, by removing discretion, in certain cases it may also negatively affect creditors. For example, financial institutions may need to write off in certain instances credit positions on their balance sheet faster, which reduces their capital buffer. Companies in those Member States that currently rely on an overindebtedness criterion would now need to file earlier for insolvency under the common liquidity trigger. To avoid that the trigger is enacted for technical (i.e. temporary), rather than structural (i.e. long-term) problems, companies in these Member States would need to adjust their business plans/cash flows to limit liquidity constraints, taking precautions for payment modalities. This leads to additional costs for these *companies*.

Debtors (i.e. companies) would benefit from clarity on the insolvency trigger primarily in the run-up to insolvency. An unclear trigger, where the court enjoys a considerable degree of appreciation/discretion, creates a situation of legal uncertainty. Once the liquidity threshold is breached, it inflicts reputational damage and will in many cases cut off the company from new financing. This accelerates the need to wind down the company and takes away (or considerably reduces) any possibility that it can remain a going concern. The setting of a clear trigger for the start of the process that leads to the liquidation of the company may, however, improve incentives for debtors to seek solutions in pre-insolvency proceedings.

In the presence of a common liquidity trigger, both *creditor* and *debtor* would be able to assess under which conditions an insolvency process starts, which should create incentives for debtors to react pre-emptively as well as for creditors to seek solutions before courts get involved. This helps avoid that the start of an insolvency procedure is postponed until the companies' position deteriorates so much that prospect of value recovery is low.

The sizeable differences in insolvency triggers across Member States imply costs to adjust to the new harmonised regime for *debtors* that have planned their business along the existing rules and for *investors* that provided finance in the knowledge of the current regime.[168] Costs for *companies* would arise from the need to implement a more sophisticated cash-flow management to contain the risk of liquidity shortfalls. These

[166] Replies in the public consultation also show a clear geographical division. Stakeholders from Member States in the North and West are on average less supportive than those in the South and East.
[167] 13% expressed a preference for a liquidity criterion in combination with a balance sheet criterion.
[168] On the concept of the costs of legal change, see Van Alstine (2002).

adjustments would likely be transitory and could be mitigated through grandfathering rules. While costs for stakeholders to adjust and to familiarise themselves with new standards may not be negiligble, they are one-off costs and their importance declines with time.

Nonetheless, the introduction of a common regime would mean a fundamental regime change in those Member States that relied on a balance sheet criterion, i.e. where insolvency was defined through overindebtedness. These Member States would also need to address tensions with other parts of law, for example if the introduction of a liquidity criterion would compromise property laws and constitutional freedoms. The reservations expressed by Member States in the public consultations to a harmonisation of insolvency triggers suggests the adjustment costs could be substantial. The adjustment costs reflect the divergences across Member States in other parts of law, than financial or insolvency laws, that govern how business is organised and contracts with other business entities are concluded/governed. These are often ruled in substantial law with links to civil law or constitutional law. Although it is not possible to provide a cost estimate for the ensuring legal uncertainty and the costs of adjusting other laws, one of the few studies in this area found that the costs of substantial changes to legislation is a multiple of those that change rules on technical proceedings.[169]

6.2.3. Measures targeting the distribution of recovered values

In addition to the elements set out in option 1, option 2 foresees a partial harmonisation of the ranking of claims.

Debtors would have broadly the same benefits and costs as in option 1. Additional benefits to *creditors* accrue from enhanced clarity about the position of some privileged creditors. Since clarity about the ranking of claims is crucial for creditors to determine their recovery value, it is a key element of insolvency regimes from their perspective.[170]

Since it is rather common that little is left to an estate after the state's claims have been fully settled, an abolishment of the privileged treatment of tax claims would allow a larger recovery value to be distributed to other unsecured creditors. Secured creditors would also appreciate that their claims become less contestable by other creditors. Their better protection should translate into a larger willingness to provide secured loans. However, changes to the ranking of creditors would entail distributional effects, which can be sizeable. The public sector would receive fewer revenues if tax claims are no longer privileged. Moreover, applying the experience of the banking sector, a rising share of secured credit can lead to asset encumbrance, implying less assets becoming disposable in insolvency cases overall (and hence to other creditors).

Any harmonisation of parts of the ranking of claims that would allow creditors to better and more easily assess, which share of the recovered value would be distributed to creditors, would be of particular benefit to *cross-border creditors*. The increase in transparency envisaged under option 1 would lead to a smaller reduction in their

[169] The estimates by Ngiem et al (2012) suggest that the costs of creating substantial legislation is about 7 times higher than that of legislation that addresses technical issues.

[170] Consistent with this view, de Guindos et al (2022) describe the ranking of claims, insolvency triggers and avoidance actions as core elements of insolvency regimes of which the harmonisation "at best practice levels" would facilitate cross-border investment.

information costs than the harmonisation of the privileges of certain creditors under option 2. This should positively affect cross-border investment.

Consistent with this argument, financial stakeholders were over-proportionally supportive towards harmonisation of the ranking of claims in their replies to the public consultation. Researchers, consultancy services and financial stakeholders were the most supportive while public authorities were the least supportive of the proposal. The responses to the public consultation, however, showed no clear (i.e. across all stakeholder groups) preference for which elements of the ranking of claims should be harmonised as a priority.[171] Stakeholders from the non-financial sector gave most support to secured credit and those from the financial sector and business services to new finance. Both correspond to their business interest as debtors, creditors and consultants, respectively. Lawyers and insolvency practitioners expressed the highest support to shareholder loans, followed by public claims. In contrast, 90% of public authorities responding to the public consultation preferred to maintain the priority status of certain claims in insolvency proceedings. Responses from public authorities were thus the most critical to the harmonisation of the elements pertaining to the treatment of public claims than any other stakeholder group.

[171] About half of the respondents ticked all possibilities: claims of secured creditors, unpaid employees, public claims, shareholder loans, new finance (multiple replies were possible).

Table 7: Key benefits and costs, by stakeholder type – Option 2 (incremental benefits/costs versus option 1

	Creditors	**Cross-border creditors/ investors**	**Insolvent company and directors (going concern)**	**SMEs**	**Employees**	**Insolvency practitioners**	**Public sector**
Benefits	- Less assets being diverted from the insolvency estate (indirect) - Less costs for the lodging of claims and participation to the insolvency proceedings (direct) - Better coordination among creditors to maximise value recovery and efficient distribution (direct) - Value maximization of distributable assets through more effective tools (pre-packs, direct)- Less uncertainty on identifying when the firm is close to insolvency (direct)	- Lower information and learning costs (costs of familiarizing themselves with the rules of the foreign regimes) through greater transparency and comparable factsheets (direct). - Easier participation and greater influcence in proceedings through standardized rules on creditors' committees (indirect)	- More certainty about when the company is insolvent (direct) - Higher chances of timely sell going concern parts of its business (indirect)	- Increased availability of an orderly liquidation for micro- and small businesses in financial distress - Debt discharge for entrepreneurs concerned by the liquidation of MSEs (automatic second chance) - Access to orderly liquidation in asset-less cases reduces moral hazard (indirect)	- Higher chances to preserve employment for going concerns parts of the business (indirect)	- Easier access to asset tracing registries (direct) - More effective tools to recover value from asset disposal (e.g. pre-pack; tools to seize assets across borders, direct)	Higher tax revenues from higher investment and productivity of the economy (indirect)
Costs	- In prepacks limited options for involvement in negotiations compared to standard restructuring - Less flexibility to address temporary liquidity problems and to preserve going concern (indirect)	- Familiarisation costs (likely small or negligible)	- Higher liability and litigation (with shareholders) risks for directors may be reflected in higher wage demands, more difficult recruitment of directors, company procedures / information flows or higher liability insurance costs (indirect) - Further internal procedures and an information flows to enable due diligence in case of a pre-pack sale (indirect) - Need for better business procedures to manage cash flows (direct and recurrent) - Familiarisation costs (likely small or negligible)	- Higher liability risks for directors and entrepreneurs (direct) - Need for better business procedures to monitor and manage cash flows (direct and recurrent) - Familiarisation costs (likely small or negligible)	- Position in ranking may be affected by the change of ranking of public claims as a consequence of harmonisation of the latter (indirect)	- Financial losses if IPs have to carry the costs in cases of asset-less companies	Fewer public revenues from less favourable treatment of public claims (direct) Need to address conflicts with other pieces of law (indirect)

The *public sector* would suffer from revenue shortfalls in those Member States where tax revenues are currently privileged and would have to be deprioritised. This might seriously affect fiscal revenues of a Member State with an insolvency backlog. At the same time, a deprioritisation of public claims would support companies' and in particular SME's access to finance since private creditors need to factor in that in case of an insolvency, their claim will be junior to those of the public sector. In those cases where the public sector steps in and pays employees' due wages, a deprioritisation of public claims would reduce the incentive for the public sector to support employees.[172]

7. HOW DO THE OPTIONS COMPARE?

7.1. Benefits and costs across the elements of insolvency regime

The introduction of the described measures under option 1 on avoidance actions, asset tracing, directors' duties, pre-packs target to preserve the best value of assets in a liquidation case and would lead to a significant improvement over the base line. The harmonisation of some key features of avoidance actions and directors' duties and the better asset tracing in cross-border cases would also provide assurances to cross-border creditors and reduce their information costs. Some measures in the option are likely to reduce the time of insolvency processes (e.g. pre-packs have a specific feature to allow for a quick approval of the sale; better asset tracing possibilities (access to registers) will also reduce the time to reclaim assets, MSE insolvency proceedings will be more proportionate). Although these measures will lead to some adjustment costs for the public sector, insolvency practitioners and companies, they should not be substantial because the targeted elements under option 1 are not expected to produce major inconsistencies with other areas of law.

A special regime for MSEs and transparency on insolvency triggers would increase the recovery value because more MSEs would be subject to an orderly liquidation and faster debt discharge. The MSE regime would be designed to deliver a shortening of the insolvency process and decrease the costs incurred for MSEs, which would both improve their situation compared to the baseline. This would also reduce debtors' incentive to procrastinate. Transparency on the insolvency triggers may not reduce the duration of the proceedings, but would rather allow creditors and debtors to better anticipate the start of insolvency and for creditors to better price the risks. These measures are likely to lead to further costs for the judicial infrastructure dealing with an increased number of MSE insolvency cases and to the public sector in charge of the production of comparable and simple yet meaningful information on insolvency regimes. But such costs are expected to be far outweighed by the benefits described above.

The primary target of more harmonised rules on creditor committees in option 1 and 2 and improved transparency on the ranking of claims in option 1 is to reduce legal uncertainty and information costs for cross-border creditors relative to the baseline. Creditor committees improve the articulation and representation of the interest of creditors with a particular benefit for cross-border creditors. It is not evident whether they would have an impact on recovery values. It is likely that they would have a positive effect on the willingness of creditors to cooperate and thus possibly reduce the length of

[172] Nevertheless, Directive 2008/94/EC, *on the protection of employees in the event of the insolvency of their employer*, guarantees a minimum level of protection for employees which is not removable by Member States.

the proceedings. While the production of the information for the transparency tool would give rise to some (limited) administrative costs mainly of one-off nature, more harmonised rules on creditor committees should not have any notable cost effects compared to the baseline.

A comprehensive EU regime (option 2) on asset recovery measures would lead to further effectiveness gains relative to the baseline because the additional elements on asset seizure and directors duties may further increase value recovery and its speed relative to option 1. The addition of asset seizure is likely to lead to a stronger impact than the addition of fiduciary duties in option 2 relative to option 1. About 75% of the insolvency experts surveyed in Deloitte and Grimaldi (2002) indicated a more than minor increase in the efficiency of insolvency cases from access to cross-border registers for the purpose of asset tracing. [173] The larger scope of option 2 would also contribute more to the reduction of legal uncertainty and information costs for cross-border investors than under option 1. The higher effectiveness with regard to the preservation of asset value and shorter insolvency proceedings would make the market exit of firms less costly under option 2. The more comprehensive coverage of elements in Option 2 would also contain the risk of forum shopping more strongly than option 1, albeit the sparse evidence that this is a material risk.[174]

New types of compliance costs would arise under both options compared to the baseline, with comparatively higher compliance costs for option 2. The harmonisation of elements at EU level would require that Member States undertake further legislative measures to restore consistency with other pieces of law (in particular under option 2, where conflicts with other areas of law are likely). In addition under option 2, courts would have to provide timely jurisprudence on the general principle of shifting the fiduciary duties for directors, at least in Member States where this principle has not existed so far. Some of the measures would increase compliance costs for companies and insolvency practitioners, which would have to comply with stricter requirements (more under option 2 than under option 1).

The more ambitious measure on insolvency triggers under option 2 may reduce legal uncertainty and information costs for cross border creditors relatively more than under option 1 and lead to earlier openings of insolvency procedures with positive effects for asset recovery and the length of proceedings. Adjustment costs for stakeholders and costs for the public sector to ensure that the harmonised insolvency trigger is consistent with other areas of national law (company and property laws) would however be substantial under option 2.

Since the ranking of claims is a major source of uncertainty, the inclusion of common rules on the ranking of claims would have a more sizeable effect on cross-border

[173] See Annex 4,Section 3.1. In the absence of data in the study by Spark and Tipik (2022) on tracing and recovery of debtor's assets by insolvency practitioners to estimate the effect of the broader and narrower coverage on asset seizure and given comparable estimates by insolvency experts in Deloitte and Grimaldi (2022) about the increase in efficiency accomplished by access to registers for the purpose of asset tracing and more powers for IPs to trace and seize assets (see chart in Annex 4), it seems a conservative assumption that the limitation to asset tracing in option 1 reduces the impact of by two thirds compared to what insolvency experts expect to result from a comprehensive solution that includes asset seizure. Regarding, directors duties, option 1 covers broadly two third of the elements of option 2, it is therefore assumed for the numerical simulation that the absence of fiduciary duties reduces the impact of directors' duties by a third.

[174] See the Spark and Tipik (2022) study on forum shopping.

creditors' legal certainty and information costs than the transparency requirements under option 1, even if the harmonisation is limited to a narrow subset of the universe of creditors. The impact of such reforms for Member States would nevertheless be sizeable because the ranking of claims touches upon the central elements of property rights and have strong implications on how the public sector will behave in the run-up to an insolvency. Apart from the risk of foregone public revenues from the deprioritisation of tax claims, the public sector may become less supportive of companies in distress, with potential far-reaching consequences for broader economic performance.

7.2. Quantification of effectiveness

The Deloitte Grimaldi survey asked insolvency practioners to assess the impact of the different measures on recovery values and time to recover. Table 8 translates these estimates into changes to the recovery rate,[175] using the EBA numbers for the average EU recovery number and time to recovery as baseline. It is shown that the recovery rate would increase by just under 2 percentage points under option 1 and almost 3 percentage points under option 2 relative to the base line. The measures on asset recovery contribute most to the higher recovery rate. Reductions in time and the saving of costs under options 1 and 2 are almost at par in their contribution to the increased recovery rate. Note, that the difference in the effect between option 1 and option 2 is largely driven by the underlying assumptions.[176]

Table 8: Induced changes to costs and time of recovery and resulting increase in the recovery rate

	Asset recovery	Insolvency procedures	Distribution of recovered assets	Sum
Option 1				
Cost savings in %	-28	-12	0	-36
Time reduction in %	-31	-13	-1	-40
Induced increase in recovery rate (%-pts)	1.02	0.38	0.02	1.42
Option 2				
Cost savings in %	-39	-12	-3	-49
Time reduction in %	-44	-13	-5	-54
Induced increase in recovery rate (%-pts)	1.56	0.38	0.13	2.07

Note: Assumptions are a recovery value of 40.4%, recovery time 3.4 years, judicial costs 1.4%, interest rate 1.36%. For more details, see Annex 4, Section 3.

[175] The present value of the recovered value net of judicial costs, see Annex 4, Section 3.1 for the formula to calculate recovery rates.

[176] The survey responses from insolvency experts could be read as the expected outcome of the most ambitious policy option. Regarding the options on pre-packs, MSEs, ranking of secured claims and creditor committees, the policy options are ambitious and therefore their indications were taken as a basis for the estimate of the impact of their realisation on the recovery rate. On avoidance actions, it is conceivable that more elements than suggested could be harmonised. Since the measure includes the core elements, an estimate that the measure yields 2/3 of the indicated effect seems conservative. Since cross-border asset tracing is a preparation to asset seizure, the table below assumes that the effectiveness of asset tracing without asset seizure in option 1 yields only 1/3 of the effect. Regarding directors' duties, option 2 is encompassing, while the absence of a change in the direction of their interest from shareholders to creditors should lead to a discount. It is assumed that the obligation to file for insolvency accounts for 2/3 of the impact on the recovery rate.

7.3. Assessment of judicial efficiency and adjustment costs

The elements discussed under both policy options would improve the efficiency and effectiveness of national judicial systems in dealing with insolvency proceedings, which is in the scope of the initiative, addressing both the first general objective and specific objectives. For example, an earlier start of proceedings (due to enhanced duties for directors to file for insolvency) as well as better means to avoid asset misuse, and better means to trace the already misused assets, should facilitate (and expedite) the work of courts and insolvency practitioners. The creation of an MSE regime is the only measure in this initiative that may lead to a possibly higher workload of courts. While these costs may be substantial in some Member States, these costs could (at least in part) potentially be outweighed by newly gained efficiencies of a more streamlined regime, which are, however, not possible to quantify. Member States would also be expected to put in place additional measures, using their discretion, to address a possible strain on court capacity due to the MSE regime.

Other measures in the competence of Member States, that they may undertake individually, or past measures already adopted, may further improve the efficiency and effectiveness of national insolvency frameworks but are considered as out of scope drivers. These could, for example, relate to setting up specialised courts (or court chambers), dedicated exclusively to insolvency proceedings, or better training of insolvency judges. In addition, there could also be additional measures that Member States can take building on recent EU law setting out rules for insolvency practitioners (e.g. on conflict of interest). Finally, any negative impact may be further mitigated by ongoing wider improvements to court proceedings, such as the upcoming digitalisation of the judicial system[177], as well as the ongoing efforts in Member States to improve the efficiency of their judicial system.

Comparing the costs of the different options is difficult. Option 1 is expected to simplify and shorten the insolvency process, and should hence reduce the costs involved. It, however, requires that the public sector adjusts the existing legal provisions and introduces transparency enhancing measures. The resulting costs for adjusting legislation in principle should not be large.[178] The introduction of the MSE regime may potentially lead to a higher burden for the judicial system if the efficiency gains from a simplified regime are outweighed by the costs from more MSE insolvency proceedings (which is not certain). In this case, higher costs for the public sector would result from granting acess to insolvency proceedings for assetless entities. Estimates of both costs to the public sector and benefits to the broader society are included in Annex 3, which also documents the assumptions used and the underlying uncertainty of the estimates.

It is expected that option 2 would lead to higher costs than option 1. All costs identified under option 1 would also be relevant under option 2. Option 2, however, gives rise to additional costs on top of those identified under option 1: the loyality conflicts between directors and shareholders, possible legal disputes in cross-border asset seizure, the need for implementation of more advanced cash-flow management by firms, short-falls for the

[177] Proposal for a Regulation laying down rules on digital communication in judicial cooperation procedures in civil, commercial and criminal matters; Proposal for a Directive aligning the existing rules on communication with the rules of the proposed Regulation.

[178] There is little data on the cost of producing legislation. A study on this topic is Ngiem et al (2012). It identified average costs of USD 2.6 million for an act in New Zealand (adopted by Parliament) and USD 382,000 for producing a regulation in New Zealand (not adopted by Parliament), and USD 980,000 for bill enacted by all US state governments.

public sector resulting from less fiscal revenue and rising asset encumbrance in insolvent firms. Some of the measures considered under option 2, notably cross-border asset seizure and a liquidity-driven insolvency trigger may lead to inconsistencies with other areas of law in some Member States. This would likely create (at least initially) a considerable degree of legal uncertainty (unlike in option 1) for stakeholders that the public sector would have to address, thus incurring substantially higher (additional) costs.[179] This is the reason why option 2 scores lower that option 1 in terms of efficiency.

7.4. Coherence with national and EU law

Discussions with insolvency experts in preparation of this impact assessment helped identify those elements, which focus on narrow and technical improvements to national insolvency rules that do not interfere with broader legal systems in Member States and the principles established in the EIR. Since option 1 is limited to these elements, it is coherent with the Member States' broader legal frameworks. The changes envisaged in option 2 would possibly lead to conflicts with the fundamental principles in other pieces of national law and necessitate costly efforts for Member States to resolve them. Option 2 therefore scores worse on coherency compared to option 1.

Both options are considered to be in full coherence with other EU legislation in this field, notably the DRI and the EIR, and address problems, which this other existing legislation does not tackle. The initiative instead focuses on the areas that were left outside the scope of the DRI, i.e. the substantive insolvency law. The two options set out in the impact assessment do not contain any changes to the areas that are affected by the implementation of the relevant provisions of the DRI.

The initiative is coherent with the Environmental Liability Directive (ELD) and does not impair the effectiveness of the ELD, which aims to limit the accumulation of environmental liabilities and to ensure compliance with the 'polluter pays' principle. ELD obliges Member States to take measures, *including financial mechanisms in case of insolvency*, with the aim of enabling operators to use financial guarantees to cover their responsibilities under ELD. These mechanisms aim to ensure that claims will be served even in cases where the debtor becomes insolvent.

7.5. Synthesis

Table 9 synthesises the qualitative and quantitative arguments in an ordinal ranking of the two policy options. Double or triple pluses or minuses were allocated when the difference from the baseline was assessed as significant or very significant in line with the reasoning in this section. They were allocated with the objective to accomplish a ranking that is consistent across the different dimensions and sub-options of options 1 and 2. The effects of suboptions were aggregated because their effects cumulate. The three dimensions of effectiveness were aggregated into an overall score through a simple average, which implies an equal weight of each dimension. The overall score is the balance of benefits (+) and costs (-).

The markings suggest that option 2 is superior to option 1 in terms of its effectiveness for value recovery and reducing legal uncertainty and information costs. However, option 1 and option 2 rank (more or less) on equal terms in their effectiveness with regard to the procedural efficiency and the distribution of recovery value, where advantages are

[179] The estimates by Ngiem et al (2012) suggest that the costs of creating substantial legislation is about 7 times higher than that of legislation that addresses technical issues.

outweighed by some disadvantages. For example, more predictable triggering of the insolvency procedure needs to be balanced against the disadvantage that the liquidity trigger removes the scope for discretionary choices from the system. Furthermore, the advantage of clarity on the ranking of public claims has largely a re-distributive impact whereas the impact on information and learning costs might be small.

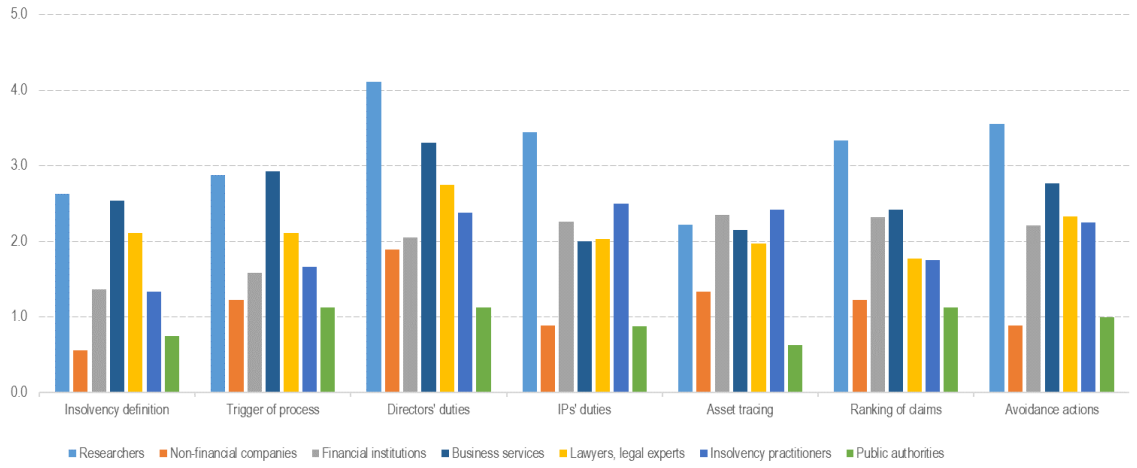
Overall, there are crucial trade-offs between the two options. Option 2 would be more effective in tackling the long-standing divergences in insolvency regimes, while it would carry higher costs and coherence issues for many Member States. In terms of effectiveness, option 2 would lead to a greater improvement of recovery rates due to more effective asset seizure and greater (overarching) liability for directors. It would also lead to a greater reduction of legal uncertainty and information costs for cross-border investors than under option 1 due to a targeted harmonisation of insolvency triggers. However, option 2 would be more costly than option 1, as it would lead to inconsistencies with the existing broader national legal systems which would imply large costs for Member States and make this option more politically challenging. For example, any harmonisation in relation to the ranking of claims in insolvency (even if limited to the treatment of public sector claims, as proposed under option 2) would have wider implications for the treatment of claims in general and raise broader issues of tax law as well as of social security legislation. Therefore, the overall advantage of option 2 over option 1 in terms of its effectiveness in achieving the objectives comes at the cost of cost-efficiency and lower coherence. Option 1 allows to achieve the objectives at lower costs and is more coherent with EU and national law, and is therefore preferred over option 2.

Table 9: Comparison of options

Objectives / Policy option	EFFECTIVENESS				EFFICIENCY (cost-effectiveness)	COHERENCE	Score
	Preserve the best possible value of assets that are due for liquidation	Support a timelier conclusion of insolvency proceedings	Reduce legal uncertainty and information costs related to insolvency processes	SUM (each objective weighted with a third)	Adjustment costs	Consistency with EU and other national laws	
Targeted measures (option 1)	**3**	**3**	**5**	**3.66**	**-2**	**0**	**1.66**
Asset recovery (avoidance actions, asset tracing, directors' duties, pre-packs)	++	+	++		-	≈	
Procedural measures: MSEs, transparency on insolvency features	+	++	+		-	≈	
Distribution of recovered assets (creditor committees and transparency on ranking)	≈	≈	++		≈	≈	
A comprehensive EU insolvency regime (option 2)	**4**	**3**	**7**	**4.66**	**-3**	**-3**	**-1.34**
Asset recovery (avoidance actions, asset tracing, directors' duties, pre-packs)	+++	+	+++		-	-	
Procedural measures: (MSEs, insolvency triggers)	+	++	++		-	-	
Distribution of recovered assets (creditor committees and targeted ranking of claims)	≈	≈	++		-	-	

The trade-off between benefits and costs also transpires in the views from stakeholders. Although the average responses to the public consultation were biased by the overrepresentation of German stakeholders, which gave a more sceptical view than those from other Member States, the breakdown by stakeholder groups in Figure 8 yields interesting insights. Researchers and representatives of business services, amongst which most were from consultancy firms, voiced overall the most supportive view. Insolvency practitioners were more ambitious in particular on some aspects of the reform (but not all), whereas public authorities advocated for a more cautious approach in almost each area. All stakeholder groups (except for public authorities) gave higher scores for the existence of a problem than for the need of reform. Financial stakeholders were overall supportive of more ambitious harmonisation than non-financial corporations, including on the ranking of claims and the insolvency trigger (part of option 2). This is consistent with the perception that the most visible benefits are likely to accrue to creditors while benefits for debtors would be more indirect and less visible, such as better access to credit.

Figure 8: Average reply by stakeholder group to the public consultation: In which area do you consider the insolvency framework of the jurisdiction where you operate is to be reformed? Scale 0-5



8. PREFERRED OPTION

Based on the comparison of effectiveness, efficiency and coherence, option 1 is selected as the preferred option. Option 1 delivers similar benefits to option 2 in terms of a shorter duration of insolvency proceedings, although a somewhat lower impact on bettervalue recovery. However, option 1 will accomplish the objectives in a more cost effective manner than potion 2. The preferred option is both internally and externally coherent. In terms of 'internal' coherence, the proposed measures fit together as they address various key phases of insolvency proceedings[180] and do so with the underlying policy objectives in mind to improve the efficiency of the insolvency proceedings and increase the recovery value.

[180] Figure 2 shows that the measures address crucial steps in an insolvency proceeding.

The measures on transaction avoidance and on asset tracing mutually reinforce each other in the maximisation of the value of the insolvency estate. This, combined with an obligation of the directors to become active early and the possibility of maximizing the value of the business at an early stage through pre-packs, makes the preservation of the business as a going concern more likely. There is, in effect, a higher likelihood that a pre-pack deal may actually materialise because there is more value and directors have a strong incentive to take action earlier. The simplified regime for MSEs could be seen as slightly less efficient than the rest, considering the potential impact on judicial capacity that was discussed above. However, it would create clear benefits for both MSEs (simplifying the review and debt discharge process) and creditors (leading to higher recovery rates), which would improve the efficiency of the overall insolvency regime to the benefit of the economy as a whole.

The preferred option is also externally coherent, by fitting well with previous EU interventions in the area of cross-border insolvency (the EIR and of preventive restructuring (the DRI). The EIR, in particular, covers the potential conflicts of laws (and jurisdictions over the proceeding) arising in cross-border insolvencies. The preferred option focuses instead on targeted harmonisation of measures for key areas of insolvency proceedings, which were not addressed previously. It therefore complements the EIR and other EU policy interventions taken over the years in the area. The comparison of options in section 7 has considered this together with the coherence with Member States' law overall.

Economic impacts

In terms of economic impacts, the preferred option is expected to bring significant benefits for creditors, companies, including SMEs, and the wider economy.

Creditors will benefit from expected higher value recovery arising from better possibilities for IPs to counter transaction avoidance and trace assets, including across borders, less asset deterioration from earlier and faster insolvency procedures and better opportunities to use pre-pack sales. Creditor committees will also allow them to more effectively coordinate their decisions. Cross-border creditors will further benefit from higher transparency on key characteristics of insolvency regimes and ranking of claims, which is expected to significantly reduce related information and learning costs.

Companies, especially those operating in a cross-border context, will face more uniform conditions and lower legal uncertainty of what will happen if they become insolvent. This sets incentives to act in time in case of financial turmoil, which increases their chance of survival. For those firms that do not manage overcoming financial distress, the more efficient framework should lead them to look for either preventive restructuring or liquidation. They benefit indirectly from the higher chances of settling parts of the business as going concern. Directors will face higher liability risks, which may lead them to demand higher wages. The initiative should not lead to higher compliance costs in general.

The initiative is expected to indirectly improve the competitiveness of the EU business sector through better prospects to wind up zombie companies. This should contribute to the reallocation of capital and labour to more productive means and hence have positive impacts on the broader economy. Since better predictability of the outcome of insolvency

procedures fosters credit provision from domestic and cross-border actors, it facilitates access to finance, which improves the competitive position of companies.

Insolvency practitioners will benefit from lower costs due to easier access to asset tracing registries and better opportunities to recover value from asset disposal. There will be a higher demand for their services due to more MSEs becoming orderly wound down. Since a share of MSE are likely to be asset-less at the time of filing for insolvency, insolvency practitioners may not be able to recover their expenses, depending on how the treatment of asset-less cases will be financed.

In terms of magnitudes, the model scenario suggests that pursuing the preferred option would reduce the cost of recovery by approximately 40% (in terms of relevant judicial costs) and the time of recovery by 50% relative to present conditions. These benefits are conditional on the good application in practice of the new rules and on that neither limited capacity in courts and IPs nor IPs abuse of their enhanced possibilities impair the performance of insolvency systems. Using the end-2021 interest rate as discount rate, the average recovery rate would increase from 37.2% to 38.7%. This implies a non-trivial improvement that results from more efficient public proceedings.

Taking the empirical estimates in Annex 4 and in the economic literature presented therein at face value, a 1.5 percentage point increase in the recovery rate could translate into a 1.5 basis point compression in debt funding costs and a 1.5 percentage point increase in intra-EU cross border portfolio asset holdings[181]. Further sizeable savings are expected in information costs for cross-border investors from more harmonised rules across Member States and from the transparency-enhancing measures.[182] Since the initiative addresses a major obstacle to capital market integration, the envisaged changes are expected to lead to a non-trivial increase in cross-border investment on the single market, with positive spill over to other policy measures under the CMU umbrella towards this end. A full harmonisation of insolvency regimes that also includes the insolvency trigger and the ranking of claims could deliver even larger gains in terms of capital market integration, as set out earlier in this impact assessment.

Impacts on SMEs

The SME test concluded that this initiative is relevant for SMEs since the dominant part of insolvency cases concern SMEs.[183] The measures in this inititative would increase the recovery rate for businesses including for SMEs. This would reduce risks for creditors and would make financing for SMEs cheaper and more easily accessible (i.e. with less or

[181] These numerical estimates result from combining coefficients and numbers from very different studies that use different methodologies, data and terminologies on a best-effort basis. Considering that this initiative addresses a very narrow determinant of cross-border capital flows and of the development of capital markets, the effects seem sizeable, but remains realistic.

[182] These are not measurable at present. Nor is it sensible to formulate a target value for recovery rates and its components. Although some Member States perform much better than others in the EBA benchmarking exercise, the lack of representativeness of the sample and its narrow focus on bank loans prevent using it to establish broader numerical targets or to assess how the expected improvement in recovery rates compares to such target.

[183] While statistics about the size breakdown of insolvent firms exists only for few Member States, SMEs represent at least 90% of the insolvency cases. See Annex 4, Section 3.

even no collateral), ceteris paribus. SMEs are even more likely to benefit from this as they are inherently more risky and hence more likely to face insolvencies.

The SMEs would also benefit directly from the creation of special insolvency regimes for MSEs that are more proportionate to their needs than the currently existing "one-size-fits-all" proceedings. It should allow more MSEs to be wound down in orderly procedures. Their improved access to orderly liquidation in asset-less cases reduces moral hazard. Entrepreneurs concerned by the liquidation of MSEs can expect easier debt discharge, which gives them a faster second chance.

The initiative does neither impose reporting burden nor compliance costs on SMEs. They would need to familiarise themselves with the new rules if they approach the state of insolvency. Under the assumption that most solvent SMEs are not familiar with insolvency rules under the current regime, these information costs should not be substantially higher than now (in fact they could be lower due to new transparency measures put forward by the initiative).

Costs related to "one in, one out"

The initiative is expected to give rise to some costs, but no cost impacts related to the 'one in, one out' approach have been identified. Costs for businesses may arise from the need to familiarise themselves with the new rules and indirectly as a result of the increased liability for directors, but these are not of administrative nature[184] Limited administrative costs are expected to arise for the Member States with the production and updating of factsheets providing greater transparency on national insolvency frameworks (since they materialise for public sectors only, these costs are out of scope of the Commission's "One-In-One-Out" commitment). Those Member States that do not yet have an electronic judicial auction platform would need to bear the cost of setting one up and those Member States that have such platform, but do not use it for insolvency cases would need to adapt them for the purpose of auctioning assets of MSEs.

Cost savings are overall expected for judicial system (insolvency lawyers and courts) as some procedures set out at a Member State level will be made simpler. Only in the second step, these will be passed on to creditors in the form of higher recovered value and then to businesses in the form of cheaper (or more accessible) financing. Hence, these costs savings, while potentially sizeable, do not count under the under Commission's "One-In-One-Out" principle. Similarly, the cost savings from a dedicated simplified insolvency procedures for MSEs relate to the simplification of national rules and not to administrative obligations under EU legislation and are therefore not counted under the "One-In-One-Out" commitment.

Annex 3 further elaborates on expected benefits and costs.

[184] These may include possible higher wage demands, more difficult recruitment of directors or higher liability insurance costs. There may also be costs for reports to directors about liability risks and information disclosure and costs about information disclosure when pre-packs are used. It was not feasible to estimate the size of these costs, although they are expected to be moderate.

Environmental impacts

No direct environmental impacts and no significant harm, either direct or indirect, are expected to arise from the implementation of the preferred option. The initiative may have some indirect positive impacts on fostering the transition to a more sustainable economy by reducing the share of zombie companies in the economy. This could enable reallocation of capital and labour towards companies with a higher rate of innovation and productivity and thus may indirectly contribute to accelerating structural change towards more sustainable production. This effect would however be indirect and is not possible to quantify. It also does not interfere with measures under the ELD. On the contrary, a more efficient insolvency framework would contribute to a speedier and more effective recovery of asset value overall and hence would facilitate the compensation of environmental claims of an insolvent company even without having recourse to financial security instruments, in full consistence with the aims of the ELD. With regards to these claims, it would partially contribute to the *predictability for investors and other economic actors* which is one of the objectives of the European Climate Law, though greater transparency on the ranking of claims – and hence this initiative is considered to be consistent with the objectives of the European Climate Law.

Social impacts

Employees are not directly impacted. The stronger incentives for entrepreneurs and directors to avoid insolvency resulting from the higher predictability of the outcome of insolvency procedures increases employees' changes to keep their jobs in going concerns parts of the business. The position in gone concern parts of the business is unchanged relative to the baseline. Often, the government compensates employees for outstanding wages and salaries. The incentive for the government to provide this compensation should not be affected by the measures. No further significant social impacts are expected.

Impact on Sustainable development goals (SDGs)

This initiative is expected to directly or indirectly contribute to the achievement of SDG no. 8 (Decent work and economic growth), SDG no. 9 (Industry, innovation, and infrastructure) and SDG no. 16 (Peace, justice and strong institutions). Annex 3 provides more detail.

Digital by default

This initiative has slightly positive impact on digitalisation, arising notably though higher degree of process automation in the simplified insolvency procedure for MSEs and use of digital portal (e-Justice portal) to provide user-friendly information on the key features of insolvency regimes and ranking of claims. Based on our assessment, it can be considered future-proof.

External impacts

While this initiative does not specifically target third countries or their entities, creditors from third countries are also expected to benefit from the measures. The benefits would materialise through the same channels as for intra-EU creditors and also the magnitude of the benefits should be comparable. As a result, more efficient and harmonised insolvency

regimes in the EU Member States could increase investment flows from abroad. The impact on the financial and the current account is, however, not quantifiable without recourse to a large set of economic assumptions.

Impact on fundamental rights

The preferred option respects the rights and principles set out in the Charter, in particular those in Article 17 (right to property), Article 16 (freedom to conduct a business), Article 15 (freedom to choose an occupation and right to engage in work), Article 47 (2) (right to a fair trial), Article 27 (Workers' right to information and consultation within the undertaking) as well as Article 8 (protection of personal data) and Article 7 (respect for private and a family life). The free movement of persons, services and establishment constituting one of the basic rights and freedoms protected by the Treaty on the European Union and the Treaty on the Functioning of the European Union is relevant for this measure.

The preferred option shall not have any negative impacts on fundamental rights since most Member States recognize that the need to safeguard the rights of creditors must be balanced against the rights of debtors and the general interest of saving companies and jobs. Fundamental rights of right to property and right to an effective remedy and to a fair trial are guaranteed under this preferred option. Overall, the impact on fundamental rights will be neutral. Although certain elements may affect the right to property and the right to an effective remedy and to a fair trial, safeguards will be foreseen in each case in order to ensure that these are proportionate in view of attaining the objectives and respect the rights and principles set out in the Charter of Fundamental Rights.

9. HOW WILL ACTUAL IMPACTS BE MONITORED AND EVALUATED?

The proposal is expected to follow normal implementation procedures for directives. Ex-post evaluation of all new legislative measures is a top priority for the Commission. The Commission shall review the outputs, results and impacts of this initiative five years after the legal instrument becomes effective.

The key indicators to measure the impact of this policy initiative in relation to the selected objectives include recovery rates, recovery time and costs of insolvency proceedings (as percentage of the recovered value). While separating the effect of the initiative from external factors will arguably be challenging and will only be possible to do in an evaluation, Commission services plan to create and monitor the following data sources that could be useful for the review:

- Recovery values and time of recovery in the enforcement of bank loans will become available from the insolvency benchmarking exercise, which the Commission committed to undertake in the 2020 CMU Action Plan. Preparations for this exercise are currently ongoing with the EBA. While this data is limited to bank loans, it is certainly an important number considering that most of companies funding is through (secured and unsecured) bank loans.
- New data on the length of procedures, and possibly the recovery rate and the size of the debtors involved in such proceedings (medium, large or micro-enterprises), as well as the outcome of the procedures opened will become available, following the adoption of an implementing act under the DRI, which imposes reporting obligations

on Member States. It will allow the Commisison to analyse the length of insolvency procedures, the breakdown of insolvencies for different sizes of companies and, dependent on Member States' ability to provide relevant data, recovery values and job losses due to insolvencies. Notwithstanding the upcoming adoption of the Commission proposal for the implementation act, it would, however, take at least several years to collect the necessary time series to perform a robust analysis of any impact.

- Surveys with insolvency and investors to gauge the effect of the different measures. It can be envisaged to run a suvey among insolvency practitioners and experts akin to the survey conducted by Deloitte/Grimaldi.
- The development of the number of insolvencies, credit volumes and costs and cross-border capital flows and home bias in international investment based on the statistics produced by Eurostat, ECB, EBA JRC and national actors (statistical offices and court statistics). These data would then be used by the Commission to analyse the impact of the intiative.

An evaluation is envisaged 5 years after the implementation of the measure and according to the Commission's better regulation Guidelines. The objective of the evaluation will be to assess, among other things, how effective and efficient it has been and to recommend whether new measures or amendments are needed.

ANNEX 1: PROCEDURAL INFORMATION

1. Lead DG, Decide Planning/CWP references

Co-lead DGs: Directorate-General for Justice and Consumers (DG JUST) and Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA)

Decide Planning: PLAN/2020/8631 – Initiative to increase the convergence of substantive corporate (non-bank) insolvency laws

2. Organisation and timing

A Commission inter-services steering group (ISSG) was established in September 2020 for preparing the initiative. It was chaired by Directorate-General Justice and Consumers (DG JUST) and was steered in close cooperation with Directorate-General for Financial Stability, Financial Services and Capital Markets Union (DG FISMA). The following DGs and services participated at the inter-service group: Legal Service (SJ), Secretariat General (SG), Directorate-General for Competition (DG COMP), Directorate-General for Economic and Financial Affairs (DG ECFIN), Directorate-General for Employment, Social Affairs and Inclusion (DG EMPL), Directorate-General for Internal Market, Industry, Entrepreneurship and SMEs (DG GROW), Directorate-General for Mobility and Transport (DG MOVE), Directorate-General for Communication (DG COMM), Directorate-General for Trade (DG TRADE), Directorate-General for Taxation and Customs Union (DG TAXUD), Directorate-General for Structural Reform Support (DG REFORM), Directorate-General for Environment (DG ENV).

Given the fact that the Insolvency initiative was included in the Commission work programme 2022, the previous ISSG was replaced, in line with the Commission working methods, with a new ISSG chaired by the Secretariat-General in November 2021. The new ISSG had the same members.

The ISSG held so far three meetings:

on 14 September 2020, where it discussed and validated the inception impact assessment report, the consultation strategy and the questionnaire to the on-line public consultation,

on 25 May 20201, where it discussed and validated the terms of reference of the external economic study supporting the preparation of the Impact Assessment by the Commission,

on 18 May 2022, where it discussed and validated the Impact Assessment report to be submitted to the RSB.

On 7 September 2022, where it discussed how the comments by the RSB were accommodated.

Another meeting of the Steering Group is scheduled to discuss and validate the Commission proposal.

3. Consultation of the RSB

Before the finalisation of the Impact Assessment report, DG JUST and DG FISMA received advice from the members of the Regulatory Scrutiny Board ("RSB") at an upstream meeting organised on 8 February 2022.

The Impact Assessment report was then examined by the Regulatory Scrutiny Board and received a negative first opinion on 24 June 2022. The Board noted a lack of evidence of how insolvency proceedings affect cross-border investment and considered the analysis of divergences across Member States as insufficient. The Board also called for a better articulation of the link of this initiative to the RDI and the EIR. It also missed an analysis of the impact on the Member States' judicial capacity, information on views of different stakeholder groups, a more balanced assessment of options and a clear presentation of the trade-offs. It asked for a more robust assessment methodology and transparency on underlying assumptions.

The Commission services revised the impact assessment in accordinace with the opinion received from the Board. More concretely, the Commission services further substantiated, where required by the Board, the elements in the core text (including by moving certain parts from the annexes), added more details about the Member States' insolvency systems in the core text as well as added methodological clarifications to the annexes. The analysis about the relationship between this initiative and the RDI, the motivation and impacts of the policy options were deepened and the presentation of methodological steps and trade-offs improved. Additional analysis was carried out on the impact of the initiative on judicial capacity in Member States and on SMEs. The views of various stakeholder groups in the public consultation were consistently added across the core text of the impact assessment (in particular, in sections 5 and 6). Tables with details about the Member States' insolvency regimes were added to annex 5, the responses to the public consultation to Annex 2 and an SME test in Annex 7. The table below presents a point-by-point list of the RSB critcisism and how it was addressed.

	RSB opinion on shortcomings	**Approach taken to resolve the shortcomings**	**Addressed in**
1a	The report does not provide sufficient **evidence of how** current insolvency proceedings negatively affect cross-border investment in the single market.	There is a rich body of assessments/reports made by international bodies, think tanks, expert groups that analysed the impact of divergent insolvency rules on the level of cross-border investment and market integration . The authors moved upfront and made more visible the evidence in this area stemming from reports of international bodies/ empirical studies that show insolvency proceedings are a crucial determinant of cross border investment and market integration.	Section 1.1; Annex 4, Section 4
		While there is no possibility to show direct empirical evidence how strongly each problem driver holds back cross-border investment and market integration, the survey data allows to establish estimates by how much targeted harmonisation of individual features would increase recovery rates and reduce recovery time. This magnitude now serves as illustration of how proceedings hold back cross-border investment/market integration.	Tables 2 and 6; Section 7.2; Annex 4, Section 3.1; in particular Table A4.9
		The text also includes now a comparison of the importance of insolvency rules as obstacle to cross border investment	Section 1.1; Annex 4,

		relative to other factors, identified by international institutions.	Section 4.4
b	It does not convincingly demonstrate why the EU should act now	The initial draft downplayed the impact of the economic downturn on the need to improve the economic adjustment capacity through more harmonised insolvency proceedings (as the forecast that insolvencies would increase once the Covid support measures ran out, did not materialise). Since the inflation pressure has mounted and the likelihood of outright recession has further increased in the meantime, these arguments were strengthened to underpin the urgency. Latest economic studies suggest that efficient insolvency rules have an important role in facilitating economic adjustment (at times of crisis/recession/recovery). This argument was made more prominent.	Sections 1.4 and 5.1
c	The analysis of **how divergent the situation is** in Member States is insufficient	More information on cross-country differences in insolvency rules has meanwhile been added to the core text. Furthermore tables with key characteristics of each problem driver for each Member States were added to Annex 5, using a study that was prepared for this purpose. Moreover, examples from Member States have been added to the description of problem drivers (i.e. which features of the building blocks exist in which Member States).	Section 1.5; Section 2.3; Annex 5
2a	The report does **not clearly set out the articulation** between the initiative and the 2019 Restructuring and Insolvency Directive	The differences between the 2019 Directive on Restructuring and Insolvency (DRI), EU Insolvency Regulation (EIR) and this initiative are now more extensively explained. It is made clear that the new initiative covers elements that the DRI/EIR do not address, since it will seek targeted harmonisation of substantive rules on insolvency.	Section 1.5 and in particular Figure 2
b	It does not clearly identify the **remaining gap** after the latter is transposed in July 2022.	The authors added a table that shows which parts of insolvency rules are not harmonised with the EIR and the DRI.	Section 1.5 and in particular Figure 2
3	The report does not sufficiently assess the **impacts on the capacity of Member State's judicial systems, resulting from the expected increased number of cases involving SMEs** and how this may affect the expected benefits.	The impact assessment now clearly says that all measures will contribute to make the insolvency regime more efficient and therewith help Member States cope with judicial capacity. The area where this is questioned by the RSB is a simplified regime for micro and small enterprises where the Board argued that the introduction of such a regime could lead to higher costs in those Member States that currently refuse opening an insolvency procedure if MSEs have too few assets to pay for the legal costs. These effects were explained more clearly in the impact assessment and estimates produced to show the effects on court capacity to the extent possible (the most exposed Member States identified).	Section 6.1.2; Section 7.3; Annex 4, Section 3.2
4a	The report does not provide a balanced assessment of options and is **geared towards the preferred option**.	The reasoning was strengthened and fine-tuned and the presentation of how both options were selected has been revised to render it more balanced. Stakeholder perspectives on the different options were also included to demonstrate that option 1 and option 2 would be favoured by different stakeholder groups. Because of its higher level of ambition option 2 is assessed as more impactful, but it also generates additional difficulties and costs that were more visibly indicated.	Section 5.2 ; Section 6.2, Chapter 7

b	It does **not present clearly the trade-offs** that policymakers face.	The text was made more explicit about the trade-offs. Option 2 would be more effective, but at the expense of higher adjustment costs and less coherence with the fundamental legal principles in Member States. Legal uncertainty during the adjustment time and higher costs for restoring legal clarity are explicitly referred to.	Section 7.5
5a	The report **does not present a robust assessment methodology** nor sets out clearly the underlying assumptions.	Assumptions were made more transparent and limitations more clearly spelled out. The description of the assessment methodology has become more transparent. The presentation was modified by summing up the three objectives into a single effectiveness criterion and by splitting efficiency and coherence into two separate criteria.	Section 7.1; Section 7.3; Section 7.5; Annex 3; Annex 4, Section 3
b	The **SME test is missing**.	An SME test was added in an additional annex. The description of the impact of an MSE regime on micro and small firms was already covered in the relevant section of the impact assessment.	Annex 7; Section 6.1.2; Annex 4, Section 3

The RSB examined the revised impact assessment and issued a positive second opinion on 10 October 2022 without reservations. The board noted that the impact assessment substantially improved, following the second submission. The board only made a very few suggestions for further improvements. Firstly, it suggested to detail more the analysis of factors that are likely to affect court capacity. Secondly, it proposed to further elaborate on the plans to collect data for future monitoring and evaluation. The final text of the impact assessment accommodated these comments to the extent possible, by adding additional detail on other factors that may influence court capacity and on data collection.

4. Evidence, Sources and Quality

In the preparation of this impact assessment, DG JUST and DG FISMA consulted a wide range of experts and stakeholders and used several different methods to gather evidence.

Evidence used in this impact assessment was gathered based on a Commission's consultation strategy, which included: (i) public feedback to the inception impact assessment; (ii) an open public consultation; (iii) a meeting with stakeholders ; and (iv) and a meeting with Member States representatives. (v) DG JUST and DG FISMA also received expertise through a collaboration with the Commission Expert Group on Restructuring and Insolvency Law consisting of both individual experts appointed in a personal capacity (so called "Type A" experts) and experts appointed to represent a common interest shared by stakeholder organisations in a particular policy area (so called "Type B" experts). The Commission held nine meetings with the expert group between April 2021 and January 2022, which helped to inform the development of policy options, especially the legislative ones. The results of all these consultation activities are presented in ANNEX 2 of this report.

DG JUST and DG FISMA also gained further insight into the subject of this report with the help of available resources, such as existing literature, reports and studies. The detailed list of these sources are to be found in the list of references at the end of this report, the list below covers only those external studies, which the Commission itself has launched for the purpose of preparing this initiative:

- Deloitte/Grimaldi (2022), Study to support the preparation of an impact assessment on a potential EU initiative increasing convergence of national insolvency laws, *Draft Final Report, DG JUST*, March 2022.
- Spark, Tipik, 'Study on the issue of abusive forum shopping in insolvency proceedings', *DG JUST*, February 2022 (specific contract nr. JUST/2020/JCOO/FW/CIVI/0160) .
- Spark, Tipik, 'Study on tracing and recovery of debtor's assets by insolvency practitioners' *DG JUST*, March 2022 (specific contract nr. JUST/2020/JCOO/FW/CIVI/0172).
- European Commission, 'Improving the evidence base on transfer of business in Europe : annex C : case study on the cross-border dimension of business transfers,' Executive Agency for Small and Medium-sized Enterprises, Publications Office, February 2021, available at: https://data.europa.eu/doi/10.2826/94014.
- Stanghellini, Mokal, Paulus, Tirado et alii, Best Practices in European Restructuring - Contractualised Distress Resolution in the Shadow of the Law , 2018.
- Steffek, F., 'Analysis of individual and collective loan enforcement laws in the EU Member States', *DG FISMA*, November 2019, available at https://ec.europa.eu/info/publications/191203-study-loan-enforcement-laws_en.
- McCormack, G. et al., 'Study on a new approach to business failure and insolvency, comparative legal analysis of the Member States' relevant provisions and practices', *DG JUST*, January 2016, available at https://op.europa.eu/en/publication-detail/-/publication/3eb2f832-47f3-11e6-9c64-01aa75ed71a1.

All of these external studies have deployed a variety of different methods for data collection, including desk research, on-line public surveys (targeted or public), structured interviews with stakeholders or validation workshops. In these studies data collection encompassed all 27 Member States, and the analytical methods used were able to deliver results in a representative manner, almost all studies are accompanied by national reports per Member States.

In general, the report was based on solid theoretical understanding gained in particular through desk research, collaboration with participants of the expert groups and research and data collection by the external contractors of the studies mentioned above. Moreover, many stakeholders have shown great interest and willingness to share their views through the consultation activities described above. The report thus draws on that thorough feedback. All EU jurisdictions were represented in the consultations.

With regard to the robustness of the data and information received, the quantitative and qualitative nature of the meaures at hand, a detailed description can be read in Annex 4 to this report.

ANNEX 2: STAKEHOLDER CONSULTATION

In line with its Consultation Strategy, the Commission carried out different and complementary consultations of stakeholders.

The **Inception Impact Assessment** was published on 11 November 2020, and received feedback from 26 stakeholders. Replies came in from various stakeholders from the financial sector, some stakeholders from the trade and industry sector, from three central governmental bodies (Portugal, Finland, Austria) and from different representatives of the insolvency practitioners, among them from the European umbrella organisation of insolvency practitioners (INSOL Europe). The feedback can be read on the dedicated website of the Commission.[185]

An **on-line public consultation** was launched in order to receive input from all the concerned stakeholders. The public consultation was launched on 18 December 2020 and after an extension of the original consultation period by more than two weeks ended on 16 April 2021. 129 contributions from 17 Member States and from the UK were submitted, with almost 45% of the responses coming in from Germany, more than 9% from Italy, 8.5% from Belgium and equally 4.65% of the responses from the Netherlands, Spain and Lithuania. One third of the replies were made on behalf of practitioners and professionals with interest in the field of insolvency (this category includes insolvency practitioners as well as lawyers). Approximatley 17% of the responses were submitted by stakeholders in the financial sector, almost 12% by stakeholders from the business and trade sector, 7% from social- and economic interest organisations and 5.5% from the members of the judiciary (judges). In addition, 10 replies (7.75%) were received from the public authorities of 8 Member States, with only 7 replies originating from the central governmental level.

As to the substance of the responses, they were in general in favour of the initiative. Stakeholders indicated that the problems created by differences in Member States' insolvency frameworks to the further development of the internal market are reasonably serious, and that differences in national insolvency frameworks deter cross-border investment/lending. According to the perception of the stakeholders, the current fragmentation affects the functioning of the internal market in particular with regard to: 1) avoidance actions; 2) the tracing and recovery of the assets belonging to the insolvency estate; 3) the duties and liability of directors in the vicinity of insolvency and 4) how insolvency proceedings are triggered. Consequently, the overwhelming majority of stakeholders were in favour of an EU action enhancing convergence in this policy field (either in form of a targeted legislation /37.21%/, as a recommendation /23.26%/, or as a combination of both /27.13%/).

As to the specific issues pertaining to insolvency law, there was widespread support (81.4%) for minimum harmonization at EU level of the duties and obligations of directors in the event of vicinity of insolvency or when the company is insolvent. Those respondents flagged, in particular, that the most beneficial aspect of harmonization would be to impose a duty on the director, once the company is insolvent, to file for insolvency

[185] https://ec.europa.eu/info/law/better-regulation/have-your-say/initiatives/12592-Insolvency-laws-increasing-convergence-of-national-laws-to-encourage-cross-border-investment_en

proceedings (70.54%). Similarly, there was widespread support amongst stakeholders for harmonisation the various aspects vis-a-vis the duties, responsibilities and powers of the IPs. With regard to the issue of ranking of claims, whereas certain areas of reform were supported (i.e. abolishing the priority status of tax and other public claims), this section saw a higher proportion of opposition to harmonisation. There was overall opposition to the proposed harmonisation of so called 'carve-out' rules (a proportion of assets recovered on the claims of secured creditors should be distributed to unsecured creditors). A number of stakeholders felt that the financial position of employees in the context of insolvency proceedings might be appropriately protected by enhancing the protections available under employment law directives, in particular, by strengthening the safeguards available under national wage guarantee funds. Furthermore, there was a wider support for a more comprehensive harmonisation of avoidance actions, encompassing the harmonisation of the different avoidance grounds, of the objective and subjective conditions leading to avoidance, as well as the time periods prior to the opening of insolvency which count as relevant for avoidance claims. Finally, respondents spoke in favour of simplifying and improving the conditions of asset tracing and recovery (e.g. 87% supported the idea that insolvency practitioners have full access to property and collateral databases)

The Commission organized a dedicated meeting with a group of selected stakeholders (on 8 March 2022). A **workshop composed of selected stakeholders** with particular interest in insolvency proceedings. The selection has been made on the basis of the scale of representation (stakeholders with European representation activity were invited). Invitees included representatives of the financial sector, the business- and trade, employees, practitioners and professionals working in insolvency proceedings, the representatives of employees and consumers, as well as academic areas and think-tanks. In the meeting, stakeholders proactively contributed by reporting on practical difficulties resulting from the fragmentation or different performance output of the national insolvency frameworks. They also expressed support towards a greater convergence in the legal landscape of insolvency proceedings in Europe.

The preparation of the initiative was supported by the **Group of experts on restructuring and insolvency law**. This Expert Group of the Commission consisting of individual experts was set up originally for the preparation of the proposal leading to the Directive on Restructuring and Insolvency. This time, the group was extended with 10 individual experts appointed as representatives of a common interest shared by shareholders in a particular policy area (the interest groups represented were financial creditors, trade creditors, consumer creditors, employee creditors, insolvent or over-indebted debtors). Between April 2021 and January 2022, the expert group held nine meetings. The detailed list of experts, as well as the meeting reports are available in the Register of Commission expert groups accessible on https://ec.europa.eu/transparency/expert-groups-register/screen/expert-groups/consult?do=groupDetail.groupDetail&groupID=3362.

In connection with the preparation of the proposal, the Commission launched and carried out **two external studies dealing with specific areas of insolvency**. Both studies were carried out by a consortium consisting of Tipik and Spark Legal Network. The first one, assessing abusive forum shopping practices in insolvency proceedings after the 2015 amendments to the EIR addresses also the question to what extent differences between

national insolvency frameworks serve as incentive for stakeholders to abusive forum shopping. The second study is dedicated to the analysis of the subject of asset tracing- and recovery in insolvency proceedings. Both studies included empirical analysis, for which data collection by the contractor involved both public on-line surveys and structured interviews with a range of stakeholders from all Member States of the EU. Both studies are available at the website of the Commission.

The Commission also **consulted Member States** in several iterations throughout the preparation of the proposal. The initiative has been addressed several time by the finance ministers of the Member States, where support was expressed towards the initiative. The Council Conclusions (ECOFIN) of 3 December 2020 on the Action Plan[186] encouraged the Commission to deliver on this initiative. These Conclusions were confirmed by the Euro Summit statement of 11 December 2020.[187] In April 2021, ministers of the Eurogroup area concluded that national reforms of insolvency regimes shall progress in coherence with parallel work streams led by EU institutions, which were undertaken in the CMU Action Plan[188]. Similarly, the statement of the Euro Summit meeting of 25 June confirmed that "structural challenges to the integration and development of capital markets, particularly in targeted areas of corporate insolvency laws, need to be identified and addressed".[189]

At the same time, given the close link of insolvency laws to other areas of national law (such as property law and labour law), and the differences concerning the main policy objectives of insolvency law, seven Member States sent a joint letter to the Commission to express reluctance to engage in substantial harmonisation discussion. Two others have separately expressed the same reluctance.

On 22 March 2022, the Commission organised a workshop with the governmental experts of the Member States in connection with the upcoming initiative. Here, Member States underlined the need for a deep and detailed problem analysis, as well as the importance of having a clear diagnosis of the actual practical problems, their scale, on the scope of stakeholders affected by them and on their actual impact on the internal market. Similarly, as to the nature of a future action at European level, these Member States reiterated their words of caution, and suggested that measures shall focus on the improvement of efficiency of insolvency proceedings.

[186] Council Conclusions on the Commission's Action Plan, doc. nr.12898/1/20 REV 1.
[187] Doc. nr. EURO 502/20.
[188] See Commission's note for the discussion at https://www.consilium.europa.eu/media/49192/20210416-eg-com-note-on-insolvency-frameworks.pdf, The summing-up letter of the discussion is available at https://www.consilium.europa.eu/media/49366/20210416-summing-up-letter-eurogroup.pdf
[189] Doc. nr. EURO 502/21.

Appendix to Annex 2: Summary report – online public consultation

1. INTRODUCTION AND OVERVIEW OF RESPONDENTS

Discrepancies in Member States' national insolvency laws create barriers to the free movement of capital in the internal market. Such discrepancies, in particular, make it more difficult to anticipate the outcome for value recovery in cases of insolvency. In 2015, the Commission concluded in its original Action Plan for a Capital Market Union that "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".

Although minimum harmonisation rules were set out by the Directive on Restructuring and Insolvency (Directive (EU) 2019/1023), significant differences continue to exist in core areas of insolvency law, such as a common definition of insolvency, the conditions for opening insolvency proceedings, the ranking of claims, avoidance actions, and the identification and tracing of assets belonging to the insolvency estate.

The present initiative complements the Directive on Restructuring and Insolvency and thus focuses on aspects of insolvency laws not addressed there.

This public consultation helped prepare this initiative by gathering the perception and views of affected stakeholders on a range of issues including: the liability and duties of directors of companies in the vicinity of insolvency; the status and duties of insolvency practitioners; the ranking of claims; avoidance actions; identification and preservation of assets belonging to the insolvency estate; core procedural notions.

Figure A2.1: Respondents to the Public Consultation questionnaire by group

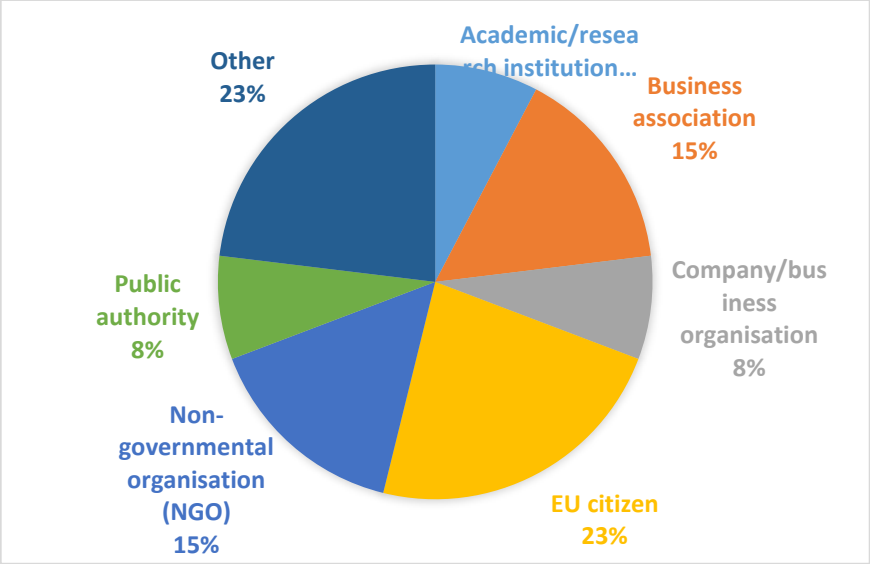


Figure A2.2: Size of organisations that responded to the questionnaire

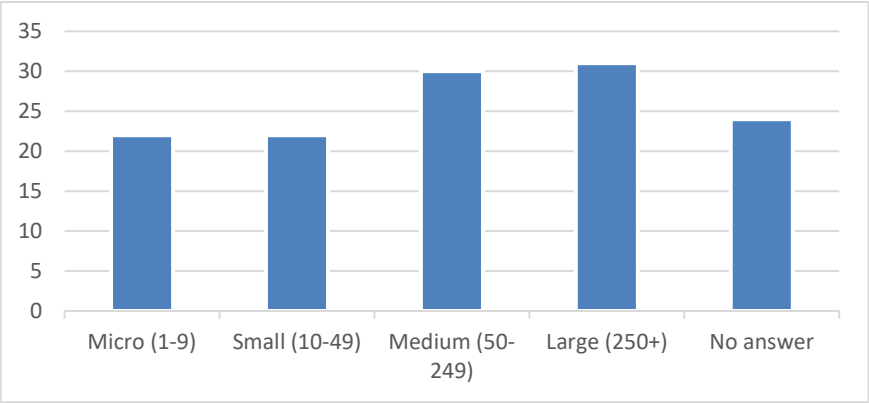
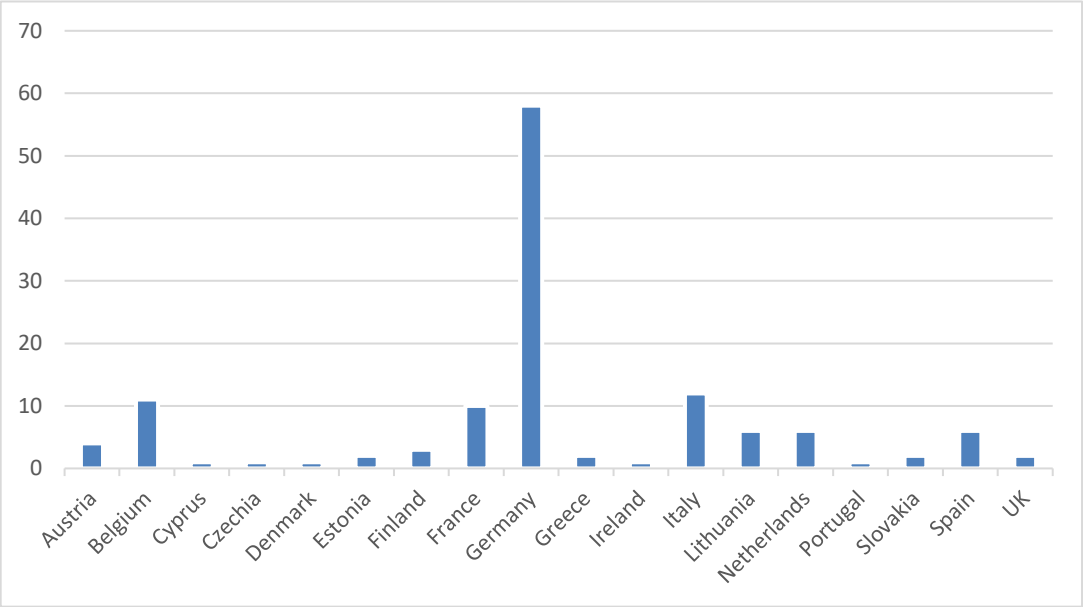


Figure A2.3. Country of origin of responses, overall



2. OUTCOME OF REPLIES

2.1. Fragmentation of insolvency frameworks and the need for greater convergence

Stakeholders indicated that the problems created for the internal market by differences in Member States' insolvency frameworks are reasonably serious, and that differences in national insolvency frameworks deter cross-border investment/lending. According to the perception of the stakeholders, the fragmentation affects the functioning of the internal market in particular with regard to 1) avoidance actions; 2) the tracing and recovery of the assets belonging to the insolvency estate; 3) the duties and liability of directors in the vicinity of insolvency and 4) how insolvency proceedings are triggered. Consequently, the overwhelming majority of stakeholders were in favour of an EU action enhancing

convergence in this policy field (either in form of a targeted legislation /37.21%/, as a recommendation /23.26%/, or as a combination of both /27.13%/).

Figure A2.4 – Assessing the scale of problems posed by differences in insolvency frameworks in the internal market. Replies in % to "Do differences in corporate (non-bank) insolvency frameworks in EU Member States pose a problem for the functioning of the internal market?" where 0 means 'no problem' and 5 means 'extremely significant problems'

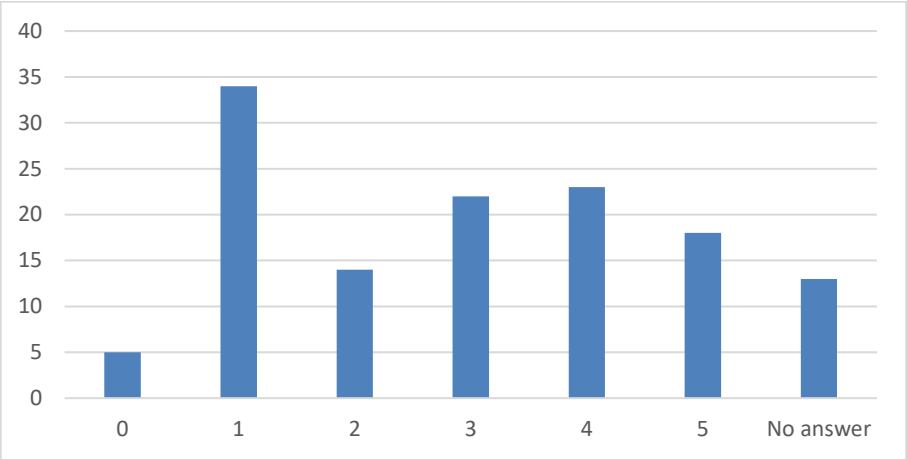
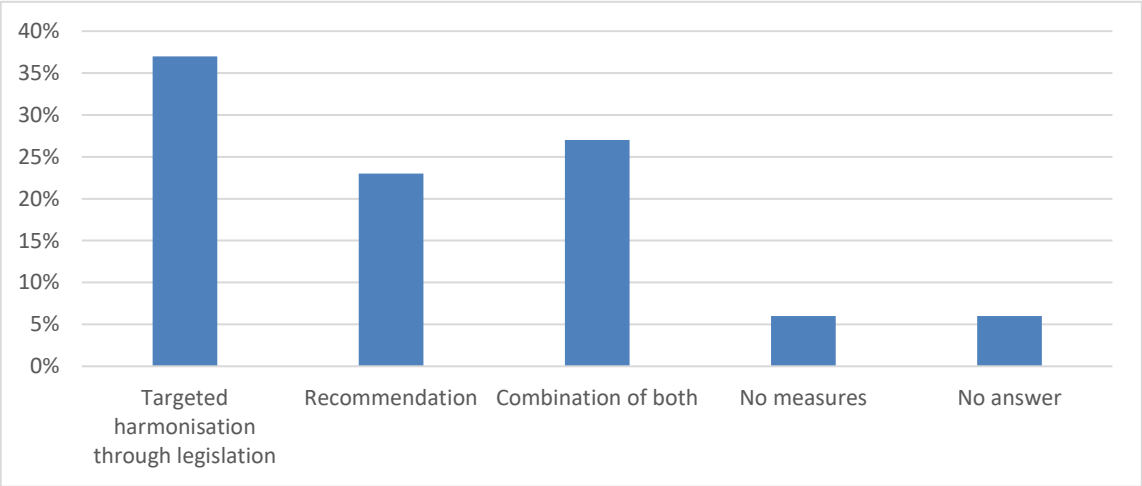


Figure A2.5 – Preferred measures to take at EU level, overall in % of respondents

The **majority of stakeholders were in favour of the introduction of legislation, either alone or in combination with a recommendation.**

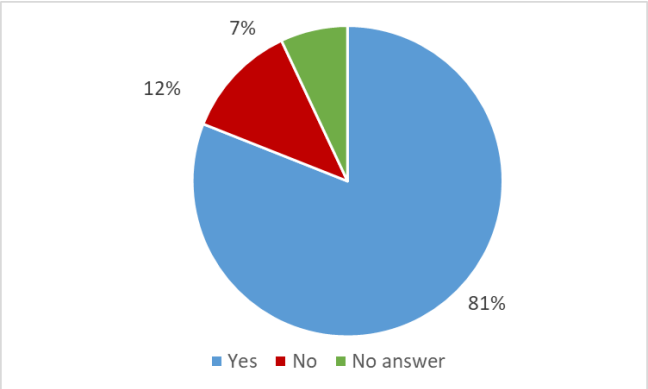


2.2. Directors' liability in the vicinity of insolvency proceedings, disqualification of directors

There is **widespread support (81%) for minimum harmonization** at EU level of the duties and obligations of directors in the event of vicinity of insolvency or when the

company is insolvent. **In particular, the most beneficial aspect of harmonization would be to impose a duty on the director, once the company is insolvent, to file for insolvency proceedings (71%).**

Figure A2.6 – On the minimum harmonisation of Directors' duties. Replies to "should there be any minimum harmonization at EU level on the duties and obligations of directors in the event of vicinity of insolvency or when the company is insolvent?



2.3. Insolvency practitioners

Overall, a majority of stakeholders felt that the following areas would benefit from harmonization at EU-level: 1) The licensing and registration of IPs (53%); 2) Their regulation, supervision and enforcement of professional obligations (51%); 3) The qualification and training of IPs (56.59%); 4) the appointment system of IPs (50%); 5) work standards and ethics (54%); and 6) the legal powers and duties of IPs (51%).

There is **considerable support for a set of principles[190] laying down parameters for the qualifications of insolvency practitioners/insolvency office holders to guide their performance of their function**, with all proposed principles gaining at least 66% support. These overlap with the areas named above, but also include the remuneration of IPs, and that IPs should be subject to a duty to keep all stakeholders regularly informed of the progress of the insolvency case.

2.4. Ranking of claims

While certain areas of reform were supported in relation to the ranking of claims (i.e. abolishing the priority status of unpaid taxes), **this section saw a higher proportion of opposition to harmonisation**. There was **overall opposition to the proposed harmonisation of carve-out rules and of rules protecting 'new-financing'**. Over one-third of academics and half of the public authorities felt that no harmonisation of insolvency law is needed regarding the position of employees in the event of insolvency. A number of stakeholders felt that the financial position of employees in the context of insolvency proceedings might be appropriately protected by enhancing the protections

[190] [1] See details in University of Leeds, "Study on a new approach to business failure and insolvency", p. 78. https://op.europa.eu/en/publication-detail/-/publication/3eb2f832-47f3-11e6-9c64-01aa75ed71a1/language-en

available under employment law directives, in particular, by strengthening the safeguards available under national wage guarantee funds.

Figure A2.7 – Less than 50% support for reform in most aspects of the rules on ranking claims- % of replies to "According to your opinion, which aspect of the rules on the ranking of claims would benefit most from a harmonization at EU level?" ˙(Multiple replies were possible.)

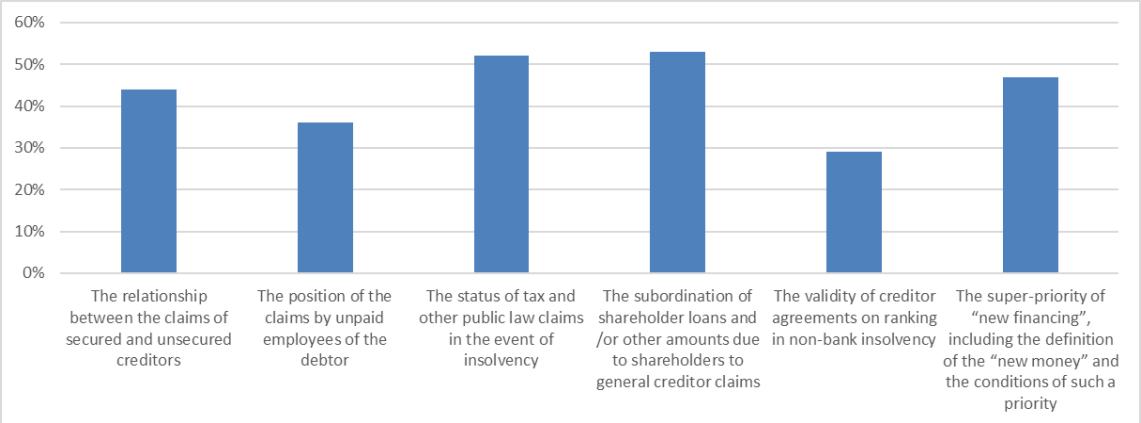
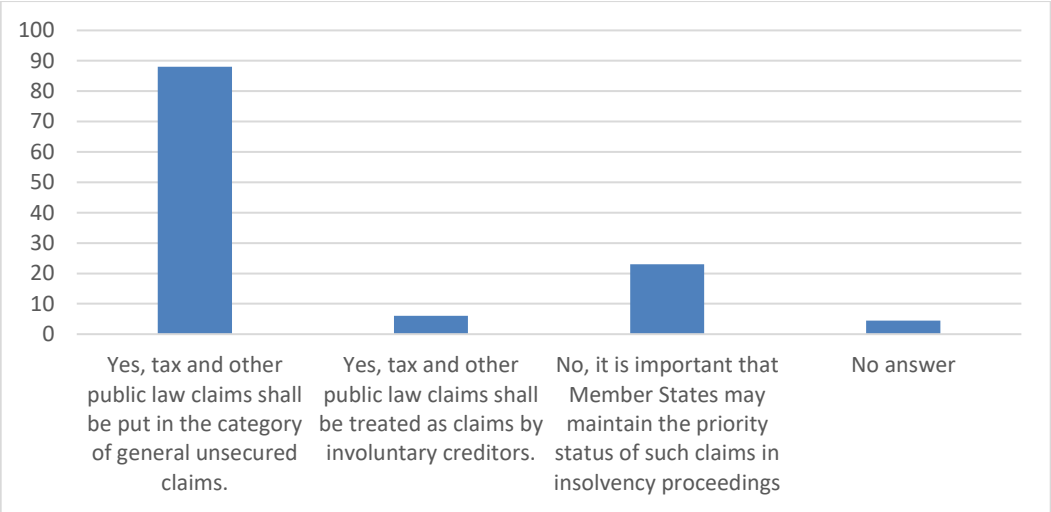


Figure A2.8 – On abolishing the priority status of unpaid taxes- % of replies to "Do you agree that the priority status of unpaid taxes and other public contributions in the context of insolvency proceedings shall be abolished at EU level?



2.5. Avoidance actions

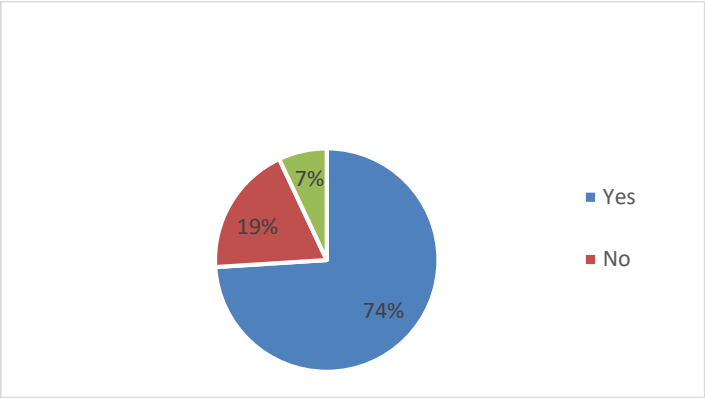
There is support for harmonized rules on avoidance action **in relation to** the following transactions: 1) **preferences** (transactions benefitting one creditor to the detriment of the general body of creditors); 2**) transactions at an undervalue**, including gifts to a creditor or third party; 3) **securities created in the 'suspect period'** in order to convert a debt from being unsecured or being secured (invalidation of securities); and 4) **transactions to defraud creditors**. Support for harmonizing the above transactions was particularly strong in the business, financial and academic sectors.

All stakeholder groups showed support for all of the proposed **subjective criteria to be used as possible conditions to qualify a transaction as avoidable action** (under

"subjective" criteria the questionnaire listed conditions which involved the subjective knowledge/awareness of the debtor/beneficiary on the real nature of the transaction). Also, the use of objective criteria was supported. The **most popular objective criteria** were that: 1) **The transaction happened within the 'suspect period' (77%)**; 2) the **transaction is to the detriment of the general body of creditors (70%)**; and 3) the **debtor was insolvent at the time of the transaction** (53%).

The majority of stakeholders (74%) agree that the 'suspect period' should be harmonized at EU level, as shown below.

Figure A2.9 – On whether the 'suspect period' should be harmonised, replies to "Should the time-periods before the opening of insolvency proceedings in which a transaction must have been entered into for it to be avoidable (the "suspect period") be harmonized at EU level?



A majority of stakeholders also support common rules on specific time-limits:

Figure A2.10 –time-limits for suspect period proposed by respondents

Transaction type	**Length: General**	**Where connected party involved**
Preferences	One year	One year
Undervalued transactions/gifts	One year/Three years	Three years
Transactions to defraud creditors	Five years	Five years

2.6. Harmonising procedural issues concerning formal insolvency proceedings

There is **support for a harmonised definition of insolvency, with the notable exception of public authorities.** The most popular proposed definition of insolvency is **based on a liquidity test** (see *Figure A2.12*). There was reasonable overall support for harmonised rules on how insolvency proceedings are opened, especially amongst practitioners. All stakeholders were strongly in favour of the idea that such rules provide creditors with a right to file for insolvency and oblige an insolvent debtor to apply for insolvency. While all stakeholder groups showed a majority support for harmonising the national rules on the time limits for creditors to lodge their claims, no clear majority emerged on a specific time limit.

Importantly, **stakeholders underlined that the national insolvency registers and the interconnectivity of national insolvency registers at EU level are not functioning properly**.

71% of stakeholders suggested that there should be harmonised rules on judges' minimum training requirements or professional qualifications (see *Figure A.2.13*). In addition, there was overwhelming support (84%) for Member States to designate specialised insolvency chambers at the appropriate court instances to increase the efficiency of insolvency proceedings (see *Fig. A2.14*).

Figure A2.11: Responses to "Should there be a harmonised definition of insolvency at EU level?"

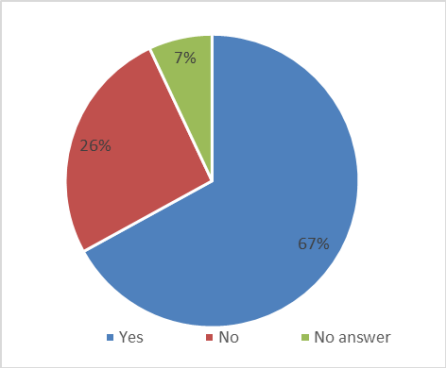


Figure A2.12: Responses to "What should the definition of insolvency be based on?"

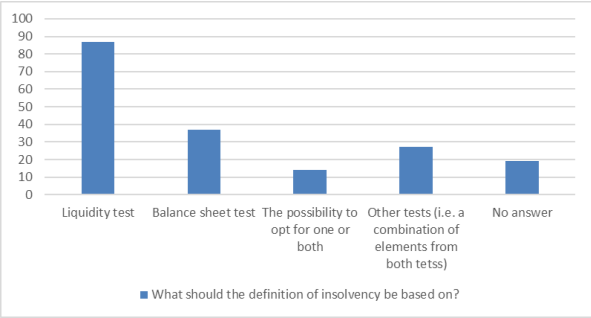


Figure A.2.13: Rules concerning judges I: Resposes to: Should the rules on minimum training requirements/professional qualifications for judges be harmonised at the EU level?"

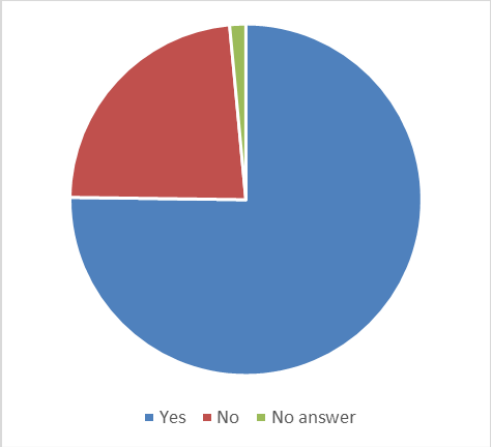
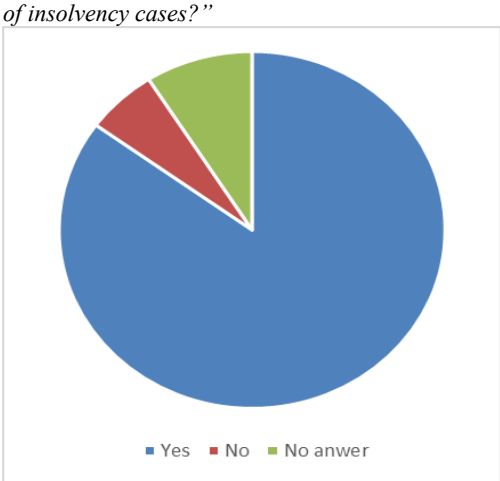


Figure A.2.14: Rules concerning judges II: 9: Responses to "Would it contribute to the efficiency of insolvency proceedings if Member States designated specialised chambers at the appropriate court instances for the handling of insolvency cases?"



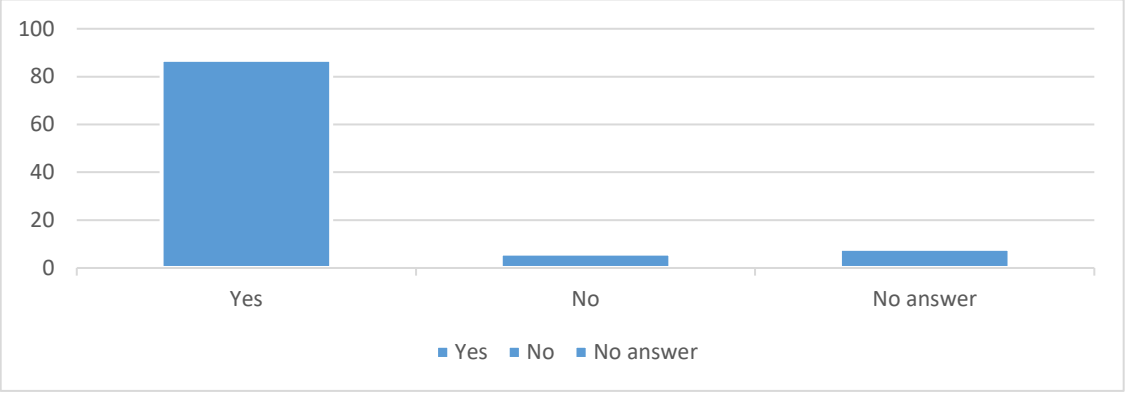
2.7. Preservation, identification and tracing of assets

All stakeholder groups support the harmonization of *ipso facto* clauses (76% overall support) to enhance legal certainty and predictability for businesses. Under *ipso facto* clauses the questionnaire understood any contractual provision that allows one party to the contract to terminate or modify the operation of the contract upon the occurrence of a specified insolvency related event. Support was especially strong amongst academics and practitioners. Furthermore, **84% of stakeholders favour harmonised rules on**

assistance (including the interconnectivity of relevant registers) in the cross-border tracing of assets of the insolvent debtor. Such rules would be most useful in relation to the following types of assets: real estate (78%), company interest (60%), bank accounts (75%) and claims (other than arising from bank accounts) (46%).

Stakeholders want insolvency practitioners to have the following powers and duties in order to trace, secure and recover assets: 1) the power to compel the production of books and records (including from lawyers, accountants and banks) (75%), 2) the power to conduct audits (65.%) and 3) the duty to report suspicious transactions to law enforcement authorities (53%). Almost all stakeholders agree that IPs should have full access to property and collateral databases.

Figure A2.15 – On giving IPs full access to property and collateral databases- replies in % to "Should Insolvency Practitioners have full access to property and collateral databases?"



3. VIEWS OF VARIOUS STAKEHOLDER CATEGORIES

This section provides a detailed analysis of the responses given to the public consultation by group of stakeholder. Since stakeholders' economic and social interests influence their views, the 129 stakeholders replies were reattributed to a functional breakdown that is closer to their economic and social background than above 2, which relies on stakeholders' self-classification.

This alternative breakdown makes use of additional information that stakeholders revealed about themselves when replying to the consultation. For some doubtful cases, stakeholders' internet websites were used to guide their attribution to a stakeholder group. Entities that responded as business and companies or their associations were distinguished into financial corporations and non-financial corporations, assuming that the former represent creditors' interest and the latter debtors' interest. Among the financial corporations are a few that specialised in debt collection, i.e. are not in the business of credit provision, but may have similar interest than for example banks. A significant number of the non-financial companies that replied to the consultation provide advisory services to other firms, i.e. consultancy, accounting and auditing. They were taken as independent third business group since their interest would be different from that of debtors. Most "EU citizens" and "other respondents" that submitted replies identified themselves as lawyers, legal experts or active as insolvency practitioners and were clustered accordingly. Four respondents represent social protection interests. The few respondents that classified themselves as EU citizens without activity as lawyer or insolvency practitioners had all academic credentials and were therefore attributed to the

group of researchers. Figure A2.16 shows the breakdown of stakeholders in the revised breakdown.

Figure A2.16: Functional breakdown of stakeholders

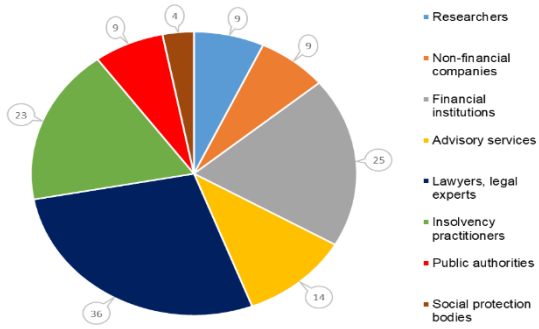
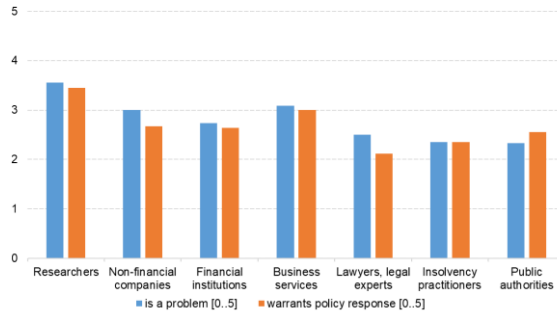


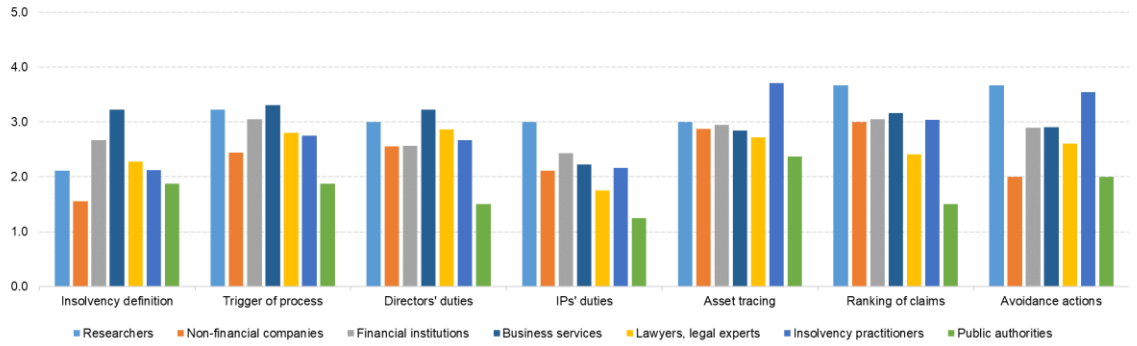
Figure A2.17: Stakeholders' assessment of the existing rules on a scale 0 to 5 with higher numbers indicating higher intensity



Respondents had comparable assessments of whether the current insolvency regimes represents a problem and would require policy measures on a scale between 0 and 5 each (Figure A2.17). Public authorities were most positive about the functioning of the current rules. They were the only group that expressed a higher need for policy action than they considered the current rules as a problem. Insolvency practitioners and lawyers were also relatively positive on the current status quo and expressed less urgency for policy measures than other stakeholder groups. Researchers were most critical on the status quo, followed by the business sector, in which those that represent interest of advisory services gave the most severe indications. Non-financial corporations gave slightly more critical marks than financial corporations, which is unexpected. None of the social protection entities responded to this question.

Figure A2.18 shows the views of the different stakeholders about which areas of insolvency law they consider the most significant barrier to the single market on a scale 0 to 5. The replies look consistent with the economic and social interest of the different stakeholder groups. Insolvency practitioners consider avoidance actions and asset tracing most severe. Financial institutions take most issues with the trigger of the insolvency process and the ranking of claims whereas non-financial business does so with asset tracing and the ranking of claims. Firms that provide advisory services flagged the insolvency definition and trigger, directors' duties and even the ranking of claims as most concerning. Researchers' put their weight on avoidance actions and the ranking of claims. None of the social protection bodies responded to this question.

Figure A2.18: Stakeholders' assessment to what extent the different elements of insolvency regimes act as a deterrent to the single market on a scale 0 to 5



Stakeholders had different views with regard to both whether EU measures were desirable in different areas (Figure A2.19) and how the EU should address the problems (Figure A2.20). Public authorities gave the least supportive responses, in particular with regard to the introduction of a common definition and common directors' duties, while their backing for asset tracing is not much lower than that of the business sector. Researchers, insolvency practitioners and legal experts were strongly supportive of EU measures that target directors' duties and asset tracing. Financial institutions gave a larger share of supportive replies to asset tracing and the introduction of a common insolvency definition. The lion's share of both financial and non-financial business supported EU measures in these three areas, with the weakest backing given to directors' duties, which is however the most important among these three areas when looking at firms that provide advice to business. Researchers and public authorities represent polar cases with respect to which instrument the EU should use. The majority of the former is in favour of a binding legal instrument, the latter group has a preference for a recommendation. The business sector holds disperse views. Advisory and financial entities place a large weight on the combination of both, similar to insolvency practitioners.

Figure A2.19: Share of stakeholders that support EU measures in three selected areas (Y/N question)

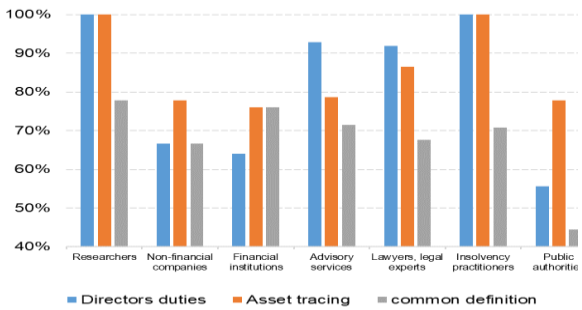
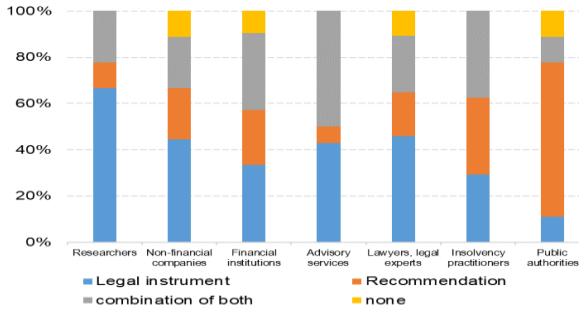


Figure A2.20: Stakeholders' assessments through which instrument the EU should act (Y/N question)



Private and public respondents expressed opposite views on the suitability of a common definition of insolvency along a liquidity criterion (Figure A2.21). Public authorities favour a combination of a balance-sheet and a liquidity criterion or the possibility to opt between both. Only a minority of the private stakeholders backs the combination or optional solution. They dominantly favour a liquidity criterion, though financial and non-financial corporations were less supportive to a liquidity criterion than the other private

stakeholder groups. Hardly any respondent, except a few legal experts favoured a balance sheet criterion.

Figure A2.21: Stakeholders' assessment of a suitable common definition of insolvency (share of respondents with positive reply, Y/N question, multiple replies possible)

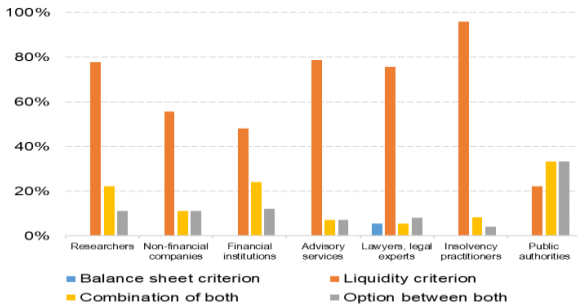
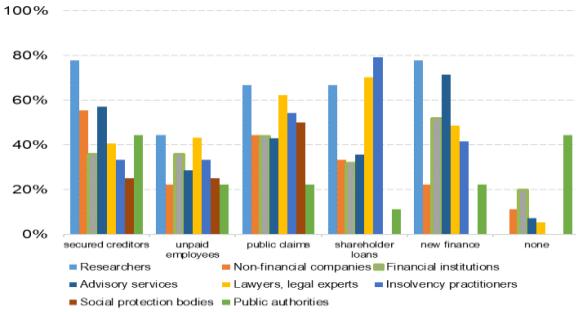


Figure A2.22: Stakeholders' assessment of credit claims that would benefit from common EU rules (share of respondents with positive reply, Y/N question)



The different views of stakeholder groups about the ranking of claims is also reflected in the variation of their views when asked which types of credit claims would benefit from common rules at EU level (Figure A2.22). Researchers are the most positive and public authorities the most negative stakeholders across the types of claims. Few of the social protection bodies that participated in the consultation see generally benefits of EU rules, not even on the claims of unpaid employees. Both financial and non-financial business express low support for common rules on the subordination of shareholder loans, while other private respondent groups do. Financial corporations' preference for common rules on new finance is shared by researchers, lawyers and insolvency practitioners. On the opposite side, non-financial companies have least interest in rules for new finance. More researchers, legal experts and insolvency practitioners see benefits from common rules on public claims than the business sector, i.e. financial, non-financial and advisory stakeholders.

Overall, perceptions of the problems suggested in the questionnaire differ across stakeholders. When asking stakeholders to what extent they see the lack of harmonised rules in the various topics of insolvency law as an impediment to the proper functioning of the internal market, public authorities and respondents belonging to the trade- and business sector did not perceive this as a significant problem (70% and 60% of the responses being in the 'less significant' range, respectively). In contrast, 69% and 55% of the insolvency practitioners or from the financial stakeholders who responded to this question saw this as a significant problem. Interestingly, the low rate of problem perception was not necessarily followed by a low rate of support for an EU harmonisation of insolvency laws. For instance, around 80% of the business- and trade sector respondents supported the idea of an EU harmonisation of the duties and obligations of directors in the vicinity of insolvency, or agreed with the abolition at EU level of the priority status of unpaid taxes in the insolvency proceedings. Similarly, more than 2/3 of them supported harmonisation on the professional regulation of insolvency practitioners or vis-à-vis avoidance actions.

ANNEX 3: WHO IS AFFECTED AND HOW?

1. Practical implications of the initiative

The preferred option will imply the following obligations for companies facing insolvency and for the Member States.

Obligations for companies facing insolvency:

Companies facing insolvency would have to familiarise themselves with the new rules and adapt some internal processes to comply. Directors would have to comply with stricter duties in the vicinity of insolvency (in particular, with the duty to timely file for insolvency). Distressed MSEs will have the option to follow a more orderly winding up based on a new simplified liquidation procedure proportionate to their needs. To be able to use it, MSEs will have to get familiar with this new regime.

Obligations for Member States

Member States would be required to further enhance transparency of the key features of their respective insolvency rules, by making such information easily accessible to investors on a public website and in a pre-defined user-friendly format. Member States would also be expected to ensure that their judicial systems make it possible for MSEs to benefit from simplified insolvency procedures and for companies to opt for a pre-pack procedure.

2. Summary of costs and benefits

The tables below summarise expected benefits and costs arising from the implementation of the preferred option (option 1) as an aggregate. The impacts of various measures can be considered additive, but not having further synergies (which could also be the case, but it may not be prudent to assume this). Main impacts summarised in the table and further information about the assumptions used are further explained below.

I. Overview of Benefits (total for all provisions) – Preferred Option		
Description	***Amount***	***Comments***
Direct benefits		
Reduction of costs to the judicial system at Member State level Who benefits: public sector (courts, insolvency practitioners)	Approximately EUR 1.9 billion of cost savings from simplification of insolvency proceedings.	The amount is obtained as 40% lower judicial costs times 1.4% judicial costs times 130 000 insolvency cases times average claim of insolvency case (see further detail below the table). This is a point estimate that is determined by these assumptions. The use of alternative assumptions leads to a higher or lower values (see text below), but it is not possible to attach probabilities to alternative scenarios.These cost savings would accrue for the judicial system (insolvency practitioners, courts) and stem from simplification of procedures at Member States level, hence they , do not count under the one in, one out commitment.
Higher recovery value Who benefits: creditors, i.e. the financial sector, the	Approximately EUR 4.9 billion out of which approximately EUR 1.9 billion are due to legal cost	A 1.42 percentage point increase (Table 8) times notional amount times 130,000 insolvency cases per annum, table in annex 4.1. The notional amount is the average claim of 2.6 million EUR derived as 3.5 million EUR average for Germany corrected for the lower GDP

public sector, other non-financial corporations and households proportional to their claims to the debtor	savings from simplification of insolvency proceedings.	per capital in the EU-27 compared to Germany (75%). Part of this are legal cost savings described above that are expected to be passed on to the creditors.
Simplified insolvency procedures for micro and small enterprises Who benefits: owners / entrepreneurs behind micro and small enterprises	Potentially sizeable, but cannot be reliably estimated.	Owners of MSEs would benefit from a dedicated simplified insolvency procedure. In most cases, this would enable an orderly winding down of distressed micro- and small businesses as costs of normal insolvency procedures were not proportionate for them. This would also accelerate debt discharge and help create a second chance for these entrepreneurs. Insolvency experts surveyed in Deloitte/Grimaldi (2022) suggest average cost savings of about 12%. EBA (2020) shows judicial costs of 3.5% for SME loans, compared to 1.4% for corporate loans.
Better coordination among creditors Who benefits: creditors, in particular cross-border creditors	Cannot be estimated	Creditor committees would allow creditors to cooperate and more effectively coordinate their decisions and would help cross-border investors to be better represented. This on one hand contributes to higher recovery value (quantified above) but also presents a benefit of its own.
Indirect benefits		
Lower debt funding costs Who benefits: companies, including SMEs	Approximately EUR 1.6 billion	Under the assumption that a 1.4% increase in the recovery rate (table 7 in section 7.2) triggers 1.4 basis points lower funding costs on 1855 billion EUR NFC liabilities in form of debt securities and EUR 9592 billion in loans 2020 (Eurostat)
Higher productivity growth Who benefits: broader society including both private and public sector	Approximately EUR 7.2 billion	0.5% higher productivity growth from fewer zombie firms (as suggested in OECD 2017), assuming insolvency rules reduce the share of zombie firms by 10%. A higher or lower share would increase respectively reduce the productivity gains proportionately, but there is no possibility to attach probabilities to different assumptions
Lower information and learning costs for cross-border investment Who benefits: cross-border creditors	Potentially sizeable, but cannot be estimated	There is neither statistical data nor a suitable methodological approach to quantify these benefits. However, based on the findings of the HLEG on CMU and stakeholder views, benefits in this area are potentially sizeable.
Higher chances of timely selling going concern parts of a distressed business Who benefits: companies, including SMEs, their investors and employees	Cannot be estimated	The harmonised pre-pack procedure would increase the chances of timely selling of going concern parts of the distressed company's business, enabling to preserve value for its shareholders and employees.
Administrative cost savings related to the 'one in, one out' approach*		
N/A[191]	N/A	N/A

[191] As explained in section 8, none of the cost savings indeitified in this table are applicable for the "one in, one out" committment.

II. Overview of costs – Preferred option							
		Citizens/Consumers		Businesses (notably insolvent businesses and creditors)		Administrations	
		One-off	Recurrent	One-off	Recurrent	One-off	Recurrent
Preferred option (as an aggregate)	Direct adjustment costs	none	none	Familiarisation with new rules (creditors, businesses at risk of insolvency, lawyers and consultants; no estimate available)	none	none	none
	Direct administrative costs	none	none	none	none	Creation of factsheets on key characteristics of insolvency frameworks: EUR 67,000-90,000[192] Development of online auction platforms and adjustment of existing platforms to iinsolvency cases: EUR 185,000-370,000[193]	Updating the factsheets - negligible costs, maintenance costs for online auction platforms: EUR 324,000 p.a.
	Direct regulatory fees and charges	none	none	none	none	none	none
	Direct enforcement costs	none	none	none	none	none	none
	Indirect costs	none	none	Further internal procedures and an information flows for distressed companies to enable due	Higher liability of directors of companies may be reflected in higher wage demands, more difficult	none	Potentially more insolvency cases, estimated at approximately EUR 0.9-2.0 billion[194] and more disputes on

[192] See below under "expected costs" for an explanation.
[193] See below under "expected costs" for an explanation.
[194] See below under "expected costs" and Annex 4, Section 3.2.

				diligence in case of pre-pack sale (conditional on company opting in for a pre-pack sale, no estimate available)	recruitment of directors, company procedures/information flows or higher liability insurance costs (no estimate available).		asset seizures (no estimate possible).
Costs related to the 'one in, one out' approach							
Total	Direct adjustment costs	none	none	Familiarisation with new rules	none		
	Indirect adjustment costs	none	none	none	none		
	Administrative costs (for offsetting)	none	none	none	none		

Relevant sustainable development goals

III. Overview of relevant Sustainable Development Goals – Preferred Option(s)		
Relevant SDG	**Expected progress towards the Goal**	**Comments**
SDG no. 8 - decent work and economic growth	Contributes to economic growth by fostering adjustment capacity and productivity. More predictable outcomes of insolvency procedures create incentives for entrepreneurs to act timely in times of economic turmoil, leading to more stable employment patterns in going concerns	Contributes directly to Target 8.3 "Promote development-oriented policies that support productive activities, decent job creation, entrepreneurship, creativity and innovation, and encourage the formalization and growth of micro-, small- and medium-sized enterprises, including through access to financial services" and indirectly to Target 8.2 "Achieve higher levels of economic productivity through diversification, technological upgrading and innovation"
SDG no. 9 – industry, innovation, and infrastructure	More efficient insolvency procedures will improve access to finance. Efficient insolvency procedures reduce the share of zombie companies and thus indirectly contribute to higher rate of innovation and productivity with a potential positive impact on accelerated structural change towards more sustainable production	Contributes indirectly to Target 9.3 "Increase the access of small-scale industrial and other enterprises to financial services, including affordable credit, and their integration into value chains and markets"
SDG no. 16 – peace, justice and strong institutions	Access to public insolvency procedure will be improved for micro and small enterprises and thus become fairer.	This contributes to Target 16.3 "Promote the rule of law at the national and international levels and ensure equal access to justice for all"

The numbers reported above are estimates based on best efforts. They do not rely on the use of a sophisticated model, but on estimates of partial effects. These estimates use the combination of financial and macroeconomic data, the Deloitte/Grimaldi survey data and assumptions which had to be used due to the inherent data limitations. The choice of the financial and macroeconomic data always had to rely on assumption on which variable is the best available proxy to the variables estimated. All the estimates are based on averages that are considered reasonable, but have to be considered as only an approximation of the individual items. Benefits and costs are expressed in economy-wide terms given that the proxy variables are mostly economy-wide and their breakdown across company sizes may not be linear.

Some critical coefficients were taken from the economic literature reviewed in Annex 4. For other coefficients, there are no means to find an approximation. The assumptions used are based on internal discussions.

The starting point for the quantitative simulations below are the figures from the EBA benchmarking exercise on the average costs and length of loan enforcement and the recovery rate in the EU. These are combined with the average response of insolvency experts in Deloitte/Grimaldi (2022) about the expected effect of harmonised EU rules on the costs and length of recovery to produce the estimates.

3. Expected benefits

Direct benefits accrue from option 1 in the form of a higher recovery rate. The lower judicial costs and faster recovery translate into a 1.42 percentage point higher recovery rate (Table 7 in section 7.2). The economy-wide benefits result from multiplying the increase in the recovery rate with the average value of the claim in an insolvency case and the number of insolvency cases. The number of insolvency cases in the EU-27 varied between 150,000 in 2019 and 100,000 in 2020. Since public support measures deflated figures in 2020 and 2021, the 2019 figures can be considered more representative for future corporate insolvencies. Since there is no data about the average value of claims in insolvency cases, the specific calculation take the number of 130,000 insolvency cases in the EU-27 and the average value of claims in Germany (EUR 3.5 million)[195] corrected for the higher GDP per capita in Germany relative to the EU-27 (75%), yielding an average value of EUR 2,600 million. The German number for the average amount was used, because it was the only number that could be identified in official statistics. Multiplying the higher recovery rate with the average value and the number of corporate insolvencies yields economy wide benefits in terms of higher recovery value from insolvency of around EUR 4.9 billion per annum.

The calculations depend on the assumptions applied. Using 100,000 or 150,000 insolvency cases and a 10% lower or higher average value of claims as alternative assumptions would produce a range for the direct economic benefits of EUR 3.4 to 6.2 billion. It appears, however, not possible to attach probabilities to the lower and higher range.

[195] Projected amount of claims divided by the number of corporate insolvency cases in 2021, German Statistical office.

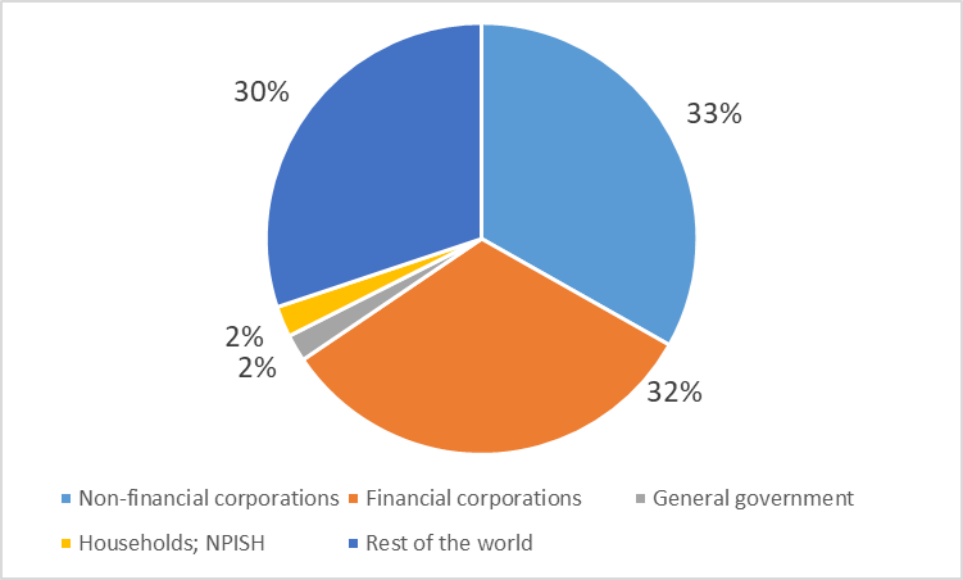
Part of the higher recovery value is due to the reduction in judicial costs by 40%. EBA (2020) reports a benchmark for judicial costs of corporate loans of 1.4% of their recovery value. Taking these costs separately to obtain a number of legal costs that can be saved, yields a value of EUR 1.9 billion admin cost savings per annum, for the 130,000 insolvency cases and taking the average value of a claim as described above. Applying the alternative set of assumptions described in the previous paragraph would lead to cost savings of EUR 1.3 as lower and 2.4 billion as upper value.

The point estimate may however represent already an underestimation of the cost savings because judicial costs are higher for SME loans at 3.5% relative to corporate loans at 1.4% and although very few Member States publish statistics about the size breakdown of insolvent firms, the available numbers suggest that they could be in the range of 90%.[196] If one assumes that the 40% cost savings apply to only 10% of the insolvent corporations and 90% of the insolvent corporations are MSEs with 3.5% judicial costs and 12% cost savings as the result of the introduction of an MSE insolvency regime as suggested by the survey responses in Deloitte/Grimaldi (2022), legal cost savings would amount to EUR 4.5 billion. These calculations demonstrate that the outcome of numerical estimates does not only depend on the underlying assumptions, but also on the degree of granularity at which the calculations are carried out.

The beneficiary of a higher recovery values would be first of all creditors, i.e. the financial sector, the public sector, other non-financial corporations and households proportional to their claims to the debtor. While the share of the recovery value will be depend on the specific situation of each insolvent corporation, the financial sector will on average be one of the the main beneficiaries given its role as credit provider to the economy. While not representative of the claims against insolvent corporations, the figure below shows how important the different institutional sectors are as creditor to the economy. The interest of the public sector is larger than the figure suggests because of two effects. First, public banks are part of the financial corporations. Secondly, tax claims are not counted as financial assets. The largest credit provider is the sector of non-financial corporations due to the important role of trade credit and other types of interfirm credit in an interlinked economy. The debtors themselves would benefit in the rare case that the lower legal costs lead the corporations to be rescued. Since corporations that have chance of being rescued should enter pre-insolvency restrucuturing procedures and not insolvency procedures, this outcome is expected to be an exceptional.

[196] The share of MSE insolvency was 91% in Germany, 95% in France and 80% in Spain.

Figure A3.1: Holdings of NFC credit liabilities by institutional sector, average of 11 Member States, 2020



Note: Calculated as sum of loans, debt securities and other accounts, non-consolidated. Average of the 11 Member States for which data is available: BG, EE, EL, FR, LV, LT, LU, HU, MT, AT, FI.
Source: FISMA calculations with Eurostat data

The public sector will be a primary beneficiary of lower legal costs, with benefits materialising in the form of lower costs for judges and court administration from more efficient and shorter proceedings. More efficient proceedings should then also translate into lower costs that are paid for insolvency practitioners, lawyers and other consultants that accompany the process and deducted from the recovered capital that is returned to creditors. The breakdown between the benefits for the public sector and these professions will be different across Member States, depending on how the judicial system is organised.

While owners of MSEs would benefit from a dedicated simplified insolvency procedure which imply cost savings for those who would otherwise use ordinary (established) insolvency procedures, these cost savings relate to simplification of national rules and not to administrative obligations under EU legislation. They can therefore not be counted under the Commission's One-In-One-Out commitment.

Indirect benefits could accrue as a result of creditors pricing in the higher expected recovery value in their demands for the interest rate they charge on debt, implying a lower interest rate, ceteris paribus. A lower interest rate means lower capital costs for the corporate sector. The magnitude of this effect is difficult to assess, but the literature surveyed in Annex 4 points to some plausible ranges. The estimates in IMF (2019) suggest that the cross-country difference in capital costs could decline by 1 basis point for a 1 percentage point higher recovery rate. AFME (2016) suggests a 3.7 base point improvement in bond spreads as consequence of a similar increase in the recovery rate. The 1 to 100 ratio looks conservative since it implies a low probability of a corporate becoming insolvent. It is also consistent with the long-term response of coefficient in the estimates in Table A4.16. Given an outstanding volume of loans by NFCs of EUR 9.6 billion and of debt securities of EUR 1.855 billion according to Eurostat's most recent

national account data, a 1.42% increase in the recovery rate in combination with the 1 to 100 translation into yields could lead to a decline of capital costs by 1.6 billion per annum.

The reallocation of capital could lead to high indirect benefits, but these can be quantified only with the help of assumptions. The OECD research presented in Annex 4 concluded that the market exit of zombie firms to the lowest share observed in a country in a sector could boost productivity growth by 0.5 percentage point. If one conservatively assumes the reform to insolvency regime contributes 10% to the market exit of zombie firms and applies this to the EU-27 GDP in 2021 productivity gains of an approximate magnitude around EUR 7 billion would be possible. If the insolvency reform contributed only 5%, the productivity gain would halve to EUR 3.5 billion and likewise if its contribution were stronger. It is, however, not possible to attach probabilities to alternative assumptions.

It was not possible to estimate the magnitude of the indirect benefits from more capital market integration due to insolvency reform and this would highly depend on the overall state of the economy. The estimates in IMF (2019a) show that cross-country risk sharing and the magnitude of cross-border assets would increase in response to an increase in recovery rates. The model simulations in Deloitte/Grimaldi suggest also a positive effect. It seems, however, not possible to produce a number for the welfare benefits in monetary terms nor to establish a number for the lower costs for information and learning.

There are further expected benefits that could not be quantified. These relate to the benefits of simplified insolvency procedures for micro and small enterprises (direct benefit), better coordination among creditors, in particular for cross-border creditors (direct benefit) and higher chances of timely selling going concern parts of a distressed business (indirect benefits). These are explained in the table above.

4. Expected costs

Additional judicial costs can arise as an indirect cost from an expected rise in insolvency cases, for example if the MSE insolvency regime leads to formal procedures for MSEs that were otherwise unwound. 9% of micro companies (with 0 or 1 employee) exit the market each year, but it is not known, how many of them would enter an insolvency proceeding, what their debt is and how many of them would have so few assets that their recovery value will be below the judicial costs of the proceeding. The estimation of possible costs needs to rely on a number of assumptions.

- The EBA (2020) benchmark points to judicial costs for SMEs are 3.5% of the notional value. Those of MSEs may be higher, but there is no information by how much. The 3.5% is therefore used as benchmark.
- The insolvency experts surveyed in Deloitte/Survey suggest that an MSE regime would reduce judicial costs by 12%. The introduction of an MSE regime in France aims to reduce judicial time by more than 50%. For the calculations, 50% is taken for the optimistic scenario and 12% for the pessimistic one. The latter is considered conservative because other cost saving effects are not taken into account, i.e. MSEs would not benefit from the 40% legal cost savings that other corporates may.
- There is no statistics about the average claims on insolvent MSEs, but an approximation of their debt can be obtained by using the share of small bank

loans to NFCs, i.e. with a volume below EUR 250,000, to total bank loans in the euro area in the ECB bank interest rate statistics as a proxy for the share of MSEs in the economy's corporate debt and multiplying this share of 12% by the outstanding loan liabilities of NFCs. The assumptions here are that MSEs have no debt in the form of debt securities and that there is no difference between them and larger firms in the proportion of loans from banks relative to non-banks.

- There is no reliable data on the share of MSE firms that enter into insolvency among those that exit the market, hence the calculation relies on an assumption.[197] IMF (2022) estimates that 9% of MSEs could become bankrupt following, which is consistent with Eurostat data showing that 8.8% of MSEs exited the market in 2019. The actual data of market exits is taken as a maximum value. The large discrepancy between market exit and insolvency declaration suggests that not all corporations that exit the market are insolvent. For a lower bound, it is therefore assumed that 2/3 of the exiting firms will use insolvency proceedings, which seems a conservative estimate given that actual insolvency numbers are less than 10% of market exits.
- There is data from Germany and Austria about the share of corporations that were rejected access to insolvency proceedings because their assets were projected not sufficient to pay for the expenses of the procedure. These two observations point to a share of about one third. It is also known from a few other Member States that the practice of rejecting insolvency applications is applied. For the EU aggregate, it is assumed that all Member States had applied this practice and would be exposed to higher costs for the judicial system from the introduction of an MSE regime that grants access to an insolvency procedure for asset-less MSEs.

Table A4.14 in Annex 4 summarises the details of the calculations and provides numbers for those Member States for which it is known that they reject applications from asset-less insolvent corporations. If all Member States applied this practice, higher costs for the judicial system would amount to between EUR 0.9 and 2 billion. The sum of the five Member States that either reject applications or immediately close proceedings for assetless corporations would be in the range EUR 0.6 to 1 billion. These calculations do not include other benefits and countervailing effects detailed in Annex 4 that are not quantifiable, but expected to lead to significant cost reductions in the judicial system.

The public sector would face costs for the creation of harmonised information on insolvency rules, which are expected to be limited and mainly of one-off nature. An IT platform that would be used already exists with e-Justice. The main cost component is therefore the production of the information. Since it concerns general rules, it should not require a legal expert not more than two weeks to produce this information. Since all 27 Member States would need to produce this information, it would take broadly one FTE per year for the EU-27. The cost figures are based on Eurostat Structure of earnings survey and Labour Force Survey data for non-wage labour costs, assuming 25% overheads. Since the precise category of lawyers was not available, the calculations work with hourly tariffs for professionals (35.6 EUR per hour) in case of lower bound and

[197] Businesses can also closed without being insolvent, for example as part of a merger, if the business purpose is fulfilled, or if the owner takes on another job.

hourly tariffs for legislators, senior officials and managers (47.8 EUR per hour) for an upper bound. It is further assumed that the average work week is 36.4 hours, obtained as the latest available EU average from Eurostat. This translates to approximately EUR 67,000-90,000 for the transparency tool.

The simplified insolvency procedures for MSEs could use electronic platforms for auctions of assets belonging to the insolvent micro enterprise. 14 Member States already have such platforms in place for online judicial auctions, but only three seem to use them for insolvency cases.[198] Member States that want to set up such a platform would need to spend resources on the development and maintenance. According to IT experts, the amounts could be EUR 5,000 -10,000 one off developments costs for a medium complex platform, plus 12,000 maintenance costs per annum. There was no information to estimate the additional costs for the specificity of using such platforms for insolvency cases. As conservative assumption, the adjustment costs could be as high as the development costs. Using these data, development cost for all those Member States that do not have a judicial platform and adjustment costs for all those that are not using it for insolvency cases would sum up to EUR 185,000 to 370,000. All 27 Member States' maintenance costs would be EUR 324,000.

Further, the higher liability placed on directors may have its own economic cost, as it might be reflected in e.g. higher wage demands, more difficult recruitment of directors or higher liability insurance costs, enhanced internal information flows. The magnitude of this indirect cost impact could be dependent on a range of factors such as labour market conditions and hence it was not possible to estimate it reliably. Further internal procedures and an information flows to enable due diligence would be needed in case the company opts-in for a pre-pack sale. This cost is considered indirect as it depends on a company's decision to find a buyer on a going concern basis. Lastly, businesses and creditors are expected to bear some costs related to becoming more familiar with new rules.

[198] According to the information of the e-justice portal..

ANNEX 4: ECONOMIC ANALYSIS

Although numerous researchers in academics and international bodies have established numerical metrics of insolvency rules and despite the successful use of many of these indicators in empirical research, their application in a study of how targeted changes to insolvency rules in the EU could impact on the outcome of insolvency proceedings and broader economic performance has turned out challenging. This text reviews the available indicators and presents a best-effort analysis to quantify the impact the discussed changes to insolvency rules could have.

For this purpose, the first section presents data on the number of corporate insolvencies and business death, complemented by various indicators that can be used as approximations for the share of cross-border insolvency cases in the absence of proper statistics on this phenomenon. The second section presents available indicators on recovery values and time. It sketches their methodological shortcomings, ultimately justifying why the World Bank and EBA data is used for the analysis. The third section translates indications from a survey among insolvency experts into changes in the recovery value of an insolvency case and establishes scenarios about magnitudes of impacts. The fourth section reports how changes to recovery rates could affect financial and macroeconomic parameters, using estimates from the empirical literature and new statistical analysis.

The combination of two empirical results allow to conclude that changes to elements of insolvency proceedings have a significant impact on cross-border investment. First, estimates for cost and time savings from the harmonisation of elements of insolvency proceedings can be derived from the indications of insolvency experts in a survey. These changes in cost and time savings can be translated into changes to recovery rates. Second, economic studies used recovery rates as indicators of insolvency rates and detected their significant impact on credit volumes, credit costs, cross-border asset holdings and risk sharing in cross-country or panel estimates. This analysis complements qualitative analysis on the impact the discussed targeted changes to insolvency rules can have on incentives of the stakeholders involved.

1. Corporate insolvencies and cross-border credit exposure

1.1 Corporate bankruptcies and market exits

Statistics of business exists and bankruptcies since 2020 are strongly influenced by the Covid-19 induced economic slowdown. Data before 2020 appear to be therefore more meaningful to inform about underlying magnitudes and trends.

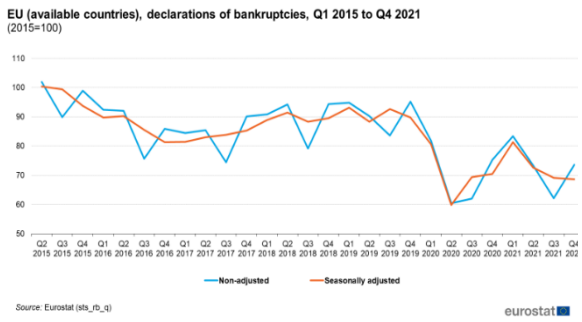
Differences in national definitions prevent Eurostat from publishing absolute numbers of bankruptcies in the EU.[199] CEPEJ (2022) contains absolute numbers of insolvency cases sourced from Member States for the years 2012-2020, but without a breakdown between corporate and consumer insolvencies. A private consultancy firm reported a number of 120,000 corporate insolvencies in Western European economies in 2020 down from

[199] In particular, the legal forms which can declare bankruptcy are different, which makes the absolute figures of the countries non-comparable.

170,000 in 2016 and a private credit insurer estimated that about 160,000 businesses might have become bankrupt in the EU Member States in 2021.[200] See the table below for numbers of corporate insolvency across the EU Member States from various sources.[201]

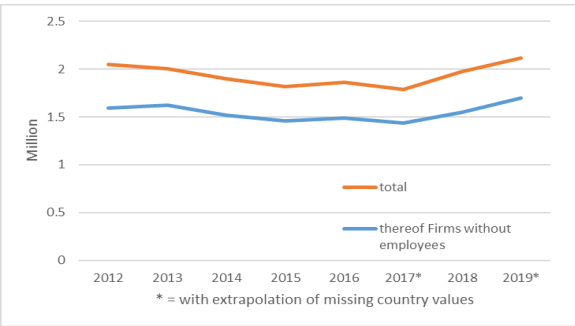
Eurostat official statistics show that the trend in the declaration of bankruptcies[202] was stable between 2015 and 2019, with a considerable drop in Q1 and Q2 of 2020, and subsequent fluctuation, as it is shown in Figure A4.1 below. The decrease in bankruptcies, observed in many Member States in the first two quarters of 2020 and the subsequent fluctuation, can be explained by the government measures supporting businesses during the beginning of the COVID-19 crisis, which allowed the businesses to avoid declaring bankruptcy.

Figure A4.1 – Business bankruptcies in the EU-27



Source: Eurostat.

Figure A4.2: Business deaths in the EU-27



Business economy except holding companies.
Source: Eurostat.

The number of deaths of EU enterprises was stable between 2014 and 2017 as it is shown in Figure A4.2, with around 1.8 million deaths per year on average. Since 2018 however, there is an increasing trend on business deaths, reaching 2.1 million in 2019. These numbers compare to a population of active enterprises in the EU of 25.9 million in 2019, which increased by around 1.5% per annum on average since 2014[203]. Almost 80% of the firms that exited in the EU in 2018[204] were firms without employees and almost 20% had 1 to 4 employees. In the EU-27, 25,000 firms with 5-9 employees exited in 2018 and 11,000 in 2017. More recent data is currently available for several Member States (see Table below).

[200] Credit Reform (Microsoft Word - 2021-05-20_AY_OE_Analyse_EU-2020_englisch.docx (creditreform.cz)) and Euler Hermes (reference Statista, Global insolvency outlook, December 2020).

[201] The CEPEJ data is not included because it also covers consumer insolvency. The number is therefore much higher than corporate insolvencies, i.e. 450,000 cases in 2019 and 257,000 cases in 2020 of 23 Member States reporting. These numbers overestimate the decline from 2019 to 2020 since there are no numbers for Germany in 2020 and none for Sweden 2019. There is also no data for the Netherlands, Cyprus, Greece in 2019 and 2020.

[202] Bankruptcies is an early indicator to measure situation in business environment. Even if an enterprise has declared for bankruptcy, it does not always mean that it ceases all activity when it enters into bankruptcy procedure. In order to be recorded as enterprise death in annual business demography typically all production factors have been dissolved / terminated. There are several methodological differences between the concepts of bankruptcies and enterprise deaths. There may also be significant differences between countries with respect to bankruptcy laws. The proportion of bankruptcy procedures that finally end up as an enterprise death varies therefore across countries depending on the bankruptcy laws. In general, bankruptcies represent only a fraction of all enterprise deaths but they cannot be directly compared with annual business demography data on deaths of enterprises.

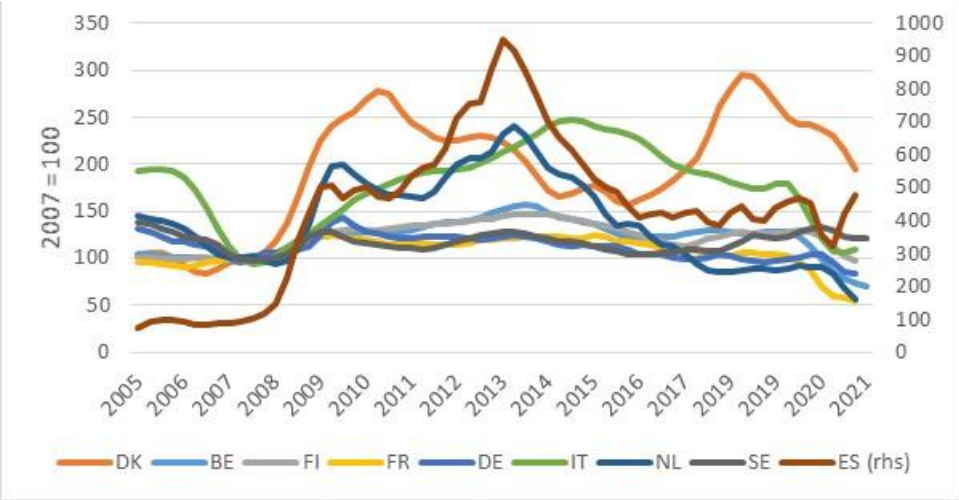
[203] An active enterprise is an enterprise that had either turnover or employment at any time during the reference period.

[204] The latest year for which aggregated data for the EU are presently available.

The comparison of about 150,000 corporate insolvencies with almost 2 million companies that cease to exist in the EU each year suggests that a substantial number of companies are wound down without recourse to public procedures. Since the latter number stems from business registers, it is not comparable with the number of insolvency cases. Yet, it shows that the use of insolvency procedures is not the standard exit route for firms. One reason is that not all firms that exit are insolvent.[205] For example, they can be acquired by or merged with other companies. The observation that 1.6 million out of 2 million or almost 80% of business deaths in the EU are companies without employees suggests that many were likely closed down because the self-employed took a job. It is also possible that companies are set up for a specific purpose and close when the company has fulfilled its purpose.[206]

Long term data from about the number of bankruptcies is available from the OECD covering the years 2005-2020 for a selected group of EU Member States. Like Eurostat, the OECD did not report absolute numbers, but an index equal to 100 in 2007.

Figure A4.3 Bankruptcy trends (index 2007 = 100)



Source: OECD.

While several countries have put in place short-term insolvency and insolvency-related measures to help ensure companies and consumers have breathing space during the crisis,[207] delaying the necessary economic adjustment is not equal of solving it. Factors such as lower sales, higher unemployment, and the transition challenge towards a greener and digital economy, point to a likely increase in the number of business insolvency filings in the near future. Last but not at least, evidence from previous crises suggest that a build-up in non-performing loans (NPL), which is related to insolvencies[208], is likely to

[205] Data from the German statistical office can illustrate the magnitude. It reported that 13,993 firms applied for an insolvency proceeding in 2021. 4.161 of them were rejected, i.e. almost 30%. This compares to more than 340,000 enterprises that exited in 2019, the latest number available in Eurostat.
[206] There is a high correlation between the birth rate and the exit rate across the EU Member States. The correlation is highest between the death rate in a year and the birth rate two years before.
[207] See Menezes and Muro (2020).
[208] See for instance Uttamachandi et al. (2021).

follow in the coming years (as NPL accumulation induced by crises usually takes several quarters to peak).

In summary, the development of corporate insolvencies in Europe in the very recent past does not reflect the true economic situation of many sectors and companies. Eventually, after crisis reaction measures cease to have effect insolvency rules will again apply with full force in all EU countries, with an expected sharp increase of cases, and the full impact of the COVID-19 related distortions will probably only become apparent in the years to come.

Table A4.1: Number of corporate insolvencies and business exits across the EU Member States

	Number of corporate insolvencies									Business exits 2019	
	2019			2020				2021			
	national sources	EH	CR	national sources	OECD	EH	CR	national sources	OECD	all firms	firms with 5 or more employees
BE	10598	10598	10598	7203	7203	11000	9878	6533	6533	25309	206
BG		506				520				103063	771
CZ	28149	8620		24903		9300				81930	342
DK	2590	2590	8474	2221	5614	3000	7155	2175	8339	27509	108
DE	18749	18749	18830	15841	15840	19500	19410	13993	13993	340535	7663
EE		148				260			103	9778	422
IE	1001.9	568	568	1054		660	767	571		#N/A	#N/A
EL	63	75	107	57	35	80	84		27	24832	#N/A
ES	4630	4162	4464	4789	4630	5000	4131			266395	7734
FR	51145	51396	51201	31259	31253	53600	53887	27639	27540	195525	2353
HR				4796				8815		22525	351
IT	11110	11000	14228	7594		13000	13695			296917	2893
CY	2374			2497				2511		3406	19
LV	221	557		516		660		838		9648	333
LT		1610				1500				49818	251
LU	1232	1445	1263	1174		1700	1195	1173		2528	132
HU	10226	5176				5850				49154	1257
MT										1776	#N/A
NL	3209	3792	3209	2703	3177	4900	3145	1536	1817	79063	315
AT	5018	5018	5235	3034		5520	5224	3034		20156	986
PL	578	977		528		1100		376		205935	3375
PT	2188	2560	5071	2216		3340	5888	1967		117677	1564
RO	6524	6524		5694		6800		6144		72364	1409
SI	1294			10125				1016		9485	71
SK	238	2447		162		2994		2994		55556	615
FI	2623	2990	2597	2135	2135	3550	2534	2472	2473	21137	298
SE	7358	7358	7296	7296	7695	8200	7599	6463	6901	44553	1174
EU*	171118.9	148866	133141	134633	77582	162034	134592	87308	67726	2136574	34642

Note: national sources are mainly statistical offices. Data for some Member States were sourced from Statista, some were traced via INSOL Europe. EH = Euler Hermes, CR = CreditReform. Data on Business exits are from Eurostat. * sum of available Member States.

1.2 The magnitude of cross border credit

The level of cross-border investment is considered as an important indication of the degree of integration of EU capital markets: although cross-border investment has increased over time as some barriers to cross-border investment have been removed, there still remains a large home bias in the EU (85% on equity investment and 69% on debt investment, see Figures A4.27 and 28). This large home bias is widely regarded as the consequence of the underdevelopment of the EU single market. Stakeholders,

researchers and institutions argue that this is to a large degree due to cross-country differences in insolvency procedures.

It is presently not possible to report a comprehensive number for the share of cross-border creditors in EU corporations.[209] Nevertheless, if such number existed, it would not show the importance of insolvency proceedings for cross-border investors since it would suffer from the same home bias. That means, it would only reflect the current situation, which is impaired by cross-border obstacles, including those on divergent and inefficient insolvency regimes.

The scale of insolvency proceedings with cross-border elements may be estimated from the proportion of outstanding foreing debt claims of MSE companies in the EU. According to the Flash Eurobarometer survey carried out in June 2016 among small and medium sized enterprises in the then 28 EU Member States, on average, 17% of those companies had debt claims against foreign debtors over 2015 fiscal year. However, in some countries this situation was much more frequent: 49% in Luxembourg, 45% in Slovenia, 31% in Austria. Half of the companies with foreign debt claims say foreign debt claims represented at least 6% in their 2015 turnover.[210]

Under the assumption that the share of cross-border bankruptcy cases is proportional to the foreign financial exposure of firms, a number of indicators allow for an approximation of the possible share of cross-border insolvencies. Overall, they suggest foreign exposures in the range of 10-20% of total credit or activity, consistent with the 17% suggested by the 2016 Eurobarometer survey (See also Figure A3.1).

The table below gives averages for the EU Member States for which data on cross-border credit exposure is available based on the latest period for which the data exists. The charts below inform about the shares for those Member States for which such ratios could be calculated. They required the combination of data from different sources, for example of NFCs liabilities in the national accounts and foreign exposure in the international investment position or of the number of enterprises in trade statistics and structural business statistics. They therefore represent an approximation.

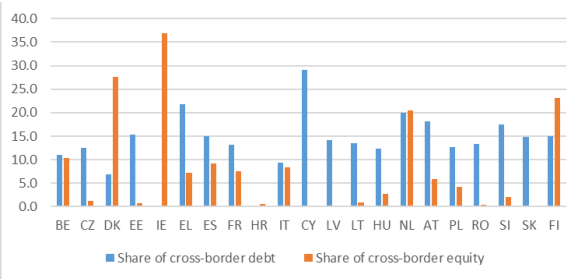
Table A4.2: Indicators to measure cross-border credit exposure

Share	**Indicator (average of available EU Member States)**	**Source, comment, caveat**
14%	Share of foreign debt in non-financial corporations, 2020	International investment position and sectoral national accounts, based on data from 20 MS
8.4%	Share of equity holdings by non-domestic holders, 2020	International investment position and sectoral national accounts, based on data from 22 MS
55%	Share of bonds issued by non-financial corporations held by non-domestic counterparts, 2020	Sectoral national accounts by counterpart, covers 11 Member States.

[210] Flash Eurobarometer, Report Insolvency, no. 442, 2016, para 1 and 2. The survey data was used in the Commission Impact Assessment Accompanying the Proposal for a Directive on preventive restructuring frameworks, second chance and measures to increase the efficiency of restructuring, insolvency and discharge procedures, SWD (2016) 357 final, p. 45.

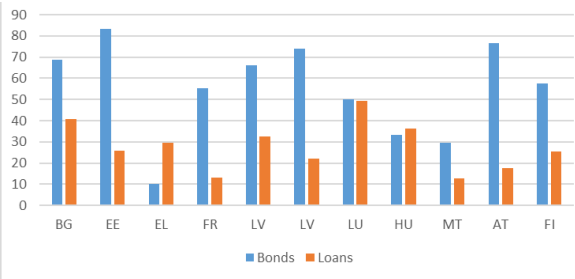
26%	Share of non-financial corporations; loan liabilities owed to non-domestic counterparts, 2020	Sectoral national accounts by counterpart, covers 11 Member States.
19%	Non-financial corporations' share of loans from banks in other Member States in total bank loans, 2022Q1	ECB data, covers only euro area Member States and banks in other euro area Member States
10%	Banks' share of loans to non-financial corporations in other Member States in total bank loans to non-financial corporations, 2022Q1	ECB data, covers only euro area Member States and banks in other euro area Member States
15%	Firms that are importers of goods or services from other EU Member States in 2019	Eurostat export and business statistics use different coverage of enterprises
64%	Firms with more than 50 employees that are importers of goods or services from other EU Member States in 2019	Eurostat export and business statistics use different coverage of enterprises
17%	Firms reporting to have claims against foreign creditors, 2016	Eurobarometer survey

Figure A4.4: Share of NFC cross-border liabilities, in % of total debt liabilities, 2020



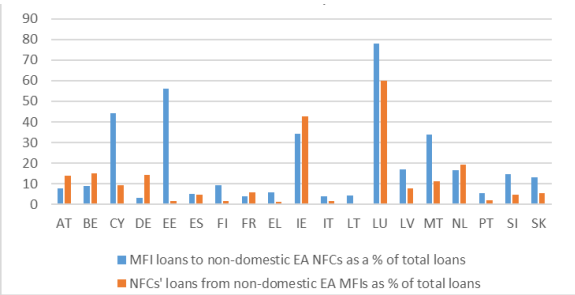
Source: FISMA calculation with Eurostat data.

Figure A4.5: Share of cross-border debt liabilities in % of total liabilities, 2020



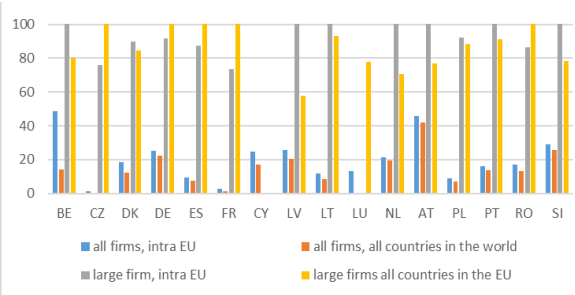
Source: FISMA calculation with Eurostat data.

Figure A4.6: Cross-border bank loans to NFCs, % of total loans to NFCs/from banks, 2021



Source: FISMA calculation with ECB data.

Figure A4.7: Share of enterprises that import, in % of all enterprises, 2019*



*) large enterprises are those with more than 250 employees. Their share is above 100% because of a different definition of entities in the export and the structural business statistics.
Source: FISMA calculation with Eurostat data.

2. Empirical measures of insolvency

The development of proper statistical data on the outcome of corporate insolvency is still in the infancy. A first comprehensive exercise towards this end by the European Banking Authority has produced numbers for the EU and its Member States. This data is not considered representative enough for cross-country analysis. Existing insolvency indicators largely build on expert views obtained from replies to surveys that largely

focus on how institutional parameters of insolvency regimes compare across countries. This holds for indicators established by the World Bank, OECD and European Commission with a varying coverage of countries.

Independent of whether these numerical metrics cover the institutional design of insolvency rules (input-oriented) or the outcome of insolvency proceedings, these indicators have been successfully used in the economic literature. That means they stand in a statistically reliable relationship to other financial and economic variables, which adds credibility to the notion that the underlying expert views are a good replacement in view of the absence of hard statistical data. Their lack of granularity, however, complicates their application for the questions analysed here. Moreover, none of them is not free from methodological caveats.

2.1 Input-oriented insolvency indicators: best-practices institutional features

Several institutions, including the World Bank, OECD, European Commission and most recently the EBRD built indicators that reflect the design of the insolvency regime in different Member States. Simply said, the input-oriented approach is based on the identification of whether best practices in insolvency law are available in a country. The more of the best practices exist in a country, the higher the indicator. The best practices and the country scores are usually established with the help of insolvency experts, either from public bodies or private entities. In most cases, the aggregate insolvency indicator reflects the count of these practices.[211] Their economic justification would be that the closer a national system to the best practices, the more efficient. The design of an input indicator as sum of desirable feature of an insolvency system assumes that interdependency between the individual feature does not matter, that improvement in individual features lead do an overall improvement in the insolvency system, without the changing being outbalanced by adverse effects in other areas or tilting the overall balance between creditors or debtors that the insolvency system in its entirety targets.

There is no space in this approach to measure the similarity of insolvency regimes across countries. This perspective is covered in empirical studies through a dummy variable that reflects the origin of the legal system, usually broken down into Anglo-Saxon, Germanic, Francophone and Nordic.[212] There is, however, also scope to make use of the indicators for a cross-country perspective when assuming that foreign investors have a preference for efficiency. That is, if cross-border investors judge the best practices as ideal insolvency system, they would be more cautious, spend more into information on the investment risk and ask for a higher risk premium the more element from the best practice are missing. Difference in best-practice elements between two countries might particularly discourage investors from a higher ranking jurisdiction as the lack of element means that these investors miss factors they are familiar with and for which they can know from domestic experiences how they work. Since the underlying policy initiative strives for convergence of insolvency proceedings towards the most efficient outcome

[211] The exception was EC (2013), which determined the weight of different components via a principal component analysis.
[212] See La Porta et al. (2008).

rather than for convergence towards a mean, there is a justification for using this approach.

Since the analysis needs to touch on elements that are much more granular than the best practices, the aggregate scores are not particular meaningful. Rather it is required to identify whether sub-components are present that cover the policy options and in a further step check whether they exist in the various Member States. The OECD indicator consists of 13 sub-component, its World Bank Doing Business (WB_DB) pendant 16 and a comparable exercise by the University of Cambridge (CBC) 4 respectively 19 subcomponents on insolvency. The European Commission conducted a similar exercise in 2018/19, asking Member States 108 questions. Although not all questions were linked to corporate insolvency, the survey led to information on whether 39 institutional features were present in their corporate insolvency system, broadly equal split between individual enforcement and insolvency proceedings. The table below shows that the elements and structures used by the four bodies presented here differ substantially. The table also reveals that many of the sub-indicators are rather remote to the issues analysed here. These are for example, those relating to individual enforcement in the EC study, those relating to restructuring by the OECD or those obtained from the latest survey carried out by the EBRD on restructuring procedures.[213]

All these data sets are publicly available except the European Commission one because it was obtained under confidentiality arrangements with Member States. While this has prevented its use by academics for empirical analysis, EBA (2020) found that some of the subcomponent are significant determinants of recovery rate and recovery time. The World Bank data set has been extensively used in the economic literature and acquired some authority. The detection of data irregularities however led to a suspension of their publication in 2020.[214] The World Bank is now engaged in a follow up project to establish new indicators.

Table A4.3: Best practices used in institutional insolvency indicators, number of sub-components in (brackets), binary except those in [square brackets show number of possibilities]

WB_DB	**CBC**	**OECD**	**EC 2013**	**EC 2019**
129 countries, 2004-2019	5 countries 1995-2005	39 countries, 2010 and 2015	EU Member States 2014	EU Member States 2019
Commencement of proceedings (3)	Entry in proceedings [3]		Ease/availability (*)	Triggers (5)
Management of debtors' assets (6)		Treatment of failed entrepreneur (3)	Continuation of operations(*)	Management of debtors' assets (6)
	Stay of secured creditors, Ranking of claims [3 and 4]		Direct and indirect costs(*)	Ranking of claims (5)

[213] EBRD 2022 structured the assessment along five dimensions: 1. General Approach to Corporate Reorganisation. 2. Planning and Initial Stage of the Reorganisation, 3. The Reorganisation Plan, 4. The Reorganisation Approval Phase, 5. Other Relevant Aspects.

[214] The irregularities in reporting information to the World Bank were found in relation to four countries, namely Azerbaijan, Saudi Arabia, United Arab Emirates and China. The review process did not identify any further specific data irregularities beyond those affecting these four countries.

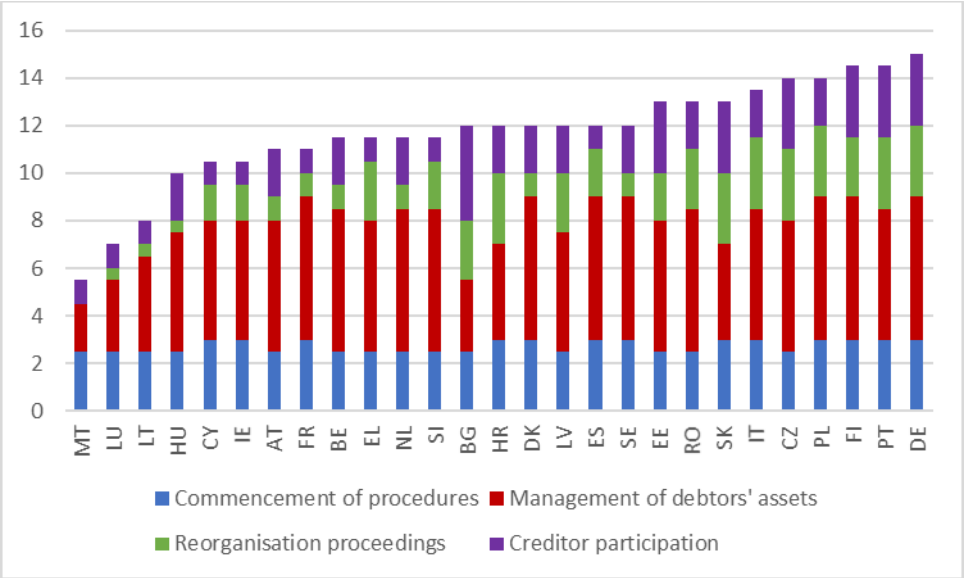
Creditor participation (4)	Creditor participation [3]			Lodgement of claims (4)
Restructuring (3)		Restructuring (5)	Debt restructuring(*)	
		Other (3)	Court capacity (6 [partly numerical])	Court capacity (4)
		Prevention and SMEs (3)		

(*) 12 institutional parameters with weights to the components allocated via principal component analysis

WB:= World Bank doing business strength of insolvency regimes, CBC:= University of Cambridge, published in Armour et al (2009), OECD indicators published in McGowan and Andrews (2018), EC 2013 is Carcea et al. (2018), EC 2019 are the indicators in Steffek (2019).

Most of the exercises yielded one-off results, which implies a limited number of observations for empirical analysis. The OECD survey was carried out in 2016 for 39 countries, the European Commission's in 2018/19 for the EU Member States. The CBC and World Bank investigations yielded time series, the CBC data ranges 1970 to 2005 for five countries with 19[215] insolvency components and 1995 to 2005 for 25 countries, the World Bank's data from 2004-2020. After the detection of data irregularities, the World Bank decided to first interrupt and later suspend updating its indicator, which means the most encompassing indicator set was discontinued in 2020.

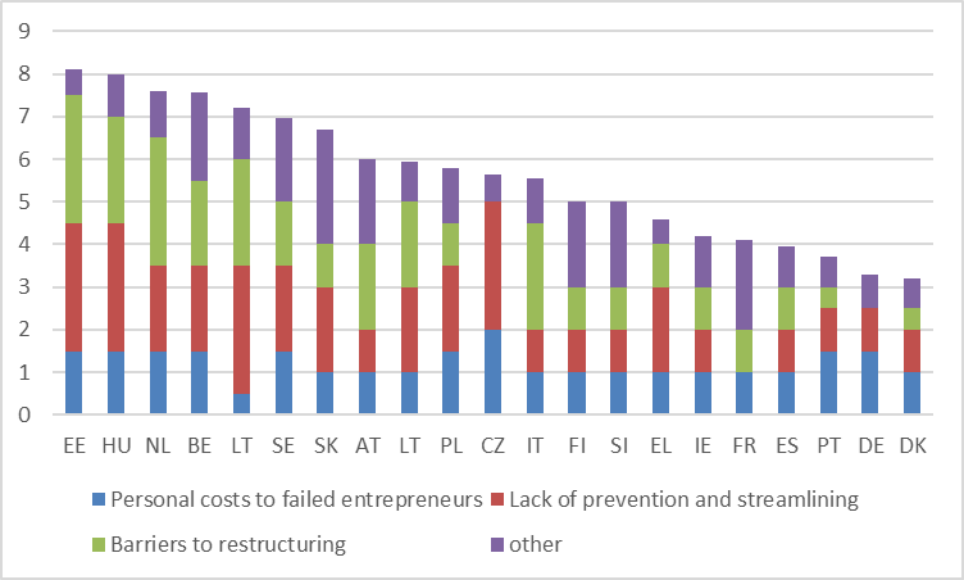
Figure A4.8: Breakdown of institutional features of insolvency regimes in the World Bank doing business indicator 2020



Note: a higher number indicates presence of more institutional features.
Source: FISMA with World Bank data.

[215] From 1970 for 5 countries (Germany, France, United Kingdom, United State of America and India).

Figure A4.9: Breakdown of institutional features of insolvency regimes in the OECD insolvency indicators 2016



Note: a higher number indicates presence of institutional features that delay the commencement and resolution of insolvency proceedings. Others relate to court involvement, distinction between honest and fraudulent bankruptcies and rights of employees.
Source: FISMA with OECD data.

The CMU context suggests a focus in the analysis on the position of foreign investors, which suggests that if specific measures of investors' information costs were available and these could be related to insolvency indicators, it would be possible to derive estimates how the different policy options would reduce information costs. Unfortunately, these gauges are not available and it has not been possible to identify other indicators to replace them. Yield differences between comparable financial instruments could be candidates. In practice, yield differences are usually found determined by differences in risk and liquidity premia. While the economic literature identified information costs as major reason for the home bias,[216] information costs are measured indirectly, i.e. through geographical distance, common language, common legal tradition, telecommunication costs etc.[217] Since the home bias is determined by other factors than information costs, it seems not suitable to use measures of home bias as proxy for information costs.

2.2 Output-oriented indicators: Recovery rates

The World Bank Doing Business indicator on insolvency was spearheaded by a group of academics that created an indicator based on the outcome of insolvency proceedings. The most important one is recovery rate that a creditor can expect to receive as return when the underlying company defaults.[218] The aggregate World Bank insolvency indicator combined such recovery rate with the institutional approach, both weighing half in the aggregate score. The recovery rate reflects the value or price of a company that enters the insolvency proceeding. When deciding on the investment, the creditor could use the

[216] See for example the literature reviewed and empirical analysis in Roque Cortez (2014).
[217] See for example, Portes and Rey (2005), Aggarwal et al. (2012).
[218] See Djankov et al. (2008).

expected recovery rate in combination with the likelihood of insolvency to establish the risk of the investment, and accordingly the risk premium requested. The standard formula for the recovery rate consists of three parameters. First, the loss of value or recovery value. This will generally be much smaller than 100%, but must not be zero because even if the borrower is insolvent, there may still be cases with a positive value. Second, the costs of insolvency proceedings, which are at least the costs for the court and administration of the insolvency. Third, the time until the recovery value is paid. The formula below shows the recovery rate RR as the present value of a payment that depends on the recovery value RV, the judicial costs C, the interest rate r and the time t until the payment is received.

$$RR = \frac{RV - C}{(1 + r)^t}$$

The recovery value RV is not a fixed, exogenously determined amount, it tends to decline the longer the duration of the process ("melting ice cube" phenomenon). Beyond the depreciation of physical assets over time, their value deteriorates if they are not used. Business lines that may still be viable on their own become less valuable if business relationships are interrupted.

RV will generally be smaller than 100%, but it is often not zero because, even if the borrower is insolvent, there may still be assets with a positive value. RV declines the longer t (so called, "melting ice cube"). The time t until the recovery value is paid, discounted by the interest rate r. The longer t, the lower RV and higher C. The costs of insolvency proceedings C are at least the costs for the court and administration of the insolvency. They also include information and legal costs for creditors.

The World Bank used this formula to calculate recovery rates for most countries of the world. It requested insolvency experts to establish for their jurisdiction what they expect these three parameters to be. Hence, the World Bank compiled data on the recovery value, the time to recovery and the costs of proceedings. To accomplish internationally comparable numbers, the insolvency experts were asked to assume a standard scenario, consisting of a hotel that went into insolvency and that creditors had secured their claim with the hotel and its interior as collateral. For the recovery value, two scenarios were assumed. Either the hotel was restructured. In this case, the recovery value would be 100% minus the depreciation of the assets times the time the insolvency procedures takes. For the calculation of the depreciation, it was assumed that the assets consisted of the furniture, with a value of 25% of the assets and that they depreciated by 20% per annum.[219] If the hotel was liquidated, the recovery value had to be estimated and could not be larger than 70%. The calculations for most EU Member States assume the hotel is restructured. The scenario of a liquidated company is used in ten smaller Member States, yielding recovery rates between 38 and 60% in the last release 2020.[220] The main criticism on the recovery rates related to the fact that the assumed scenario of a hotel was not representative for other corporations. The methodology came also under criticism when it appeared that calculations for some countries were politically influenced, which led to the suspension of the Doing Business indicators. That said the Doing Business

[219] When introduced into the formula RV would be 100-25*20%*t in case of restructuring.
[220] These were BG, EL, EE, HR, MT, HU, LV, LT, LU, RO and until 2015 SI.

recovery rates performed well when academics or staff from international organisations used them in empirical analysis.

Credit rating agencies and banks collect information about actual recovery rates from their daily business, with credit rating agencies having their strengths in corporate bonds and banks in corporate loans. Although the business model of credit rating agencies consists in assessing the likelihood and consequences of default, their information base is limited. For example, the data base of a major credit rating agency analysed for this exercise reported about 110 cases of default per year on average 2017-2021, of which 21 from European entities. The information from this credit rating agency points to recovery rates being volatile over time and depending on the type of financial securities. For example, recovery rates of secured senior bonds[221] varied between 50 and 70% in the period 2017-2021, those of unsecured bonds between 30 and 50%. These numbers relate to global markets. When looking at US markets, the recovery rate of secured loans varied between 50 and 82% in the period 2017-2021. The difference in the recovery rate of these loans to unsecured bonds moved in the range between 0 and 25%. The variation seems rather large compared to what one would expect if the only influential factor were the business cycle. This suggests the composition of the panel has also an important influence.

It would be possible to calculate statistics on the expected recovery rate as a function of the yield difference of a corporate bond or credit default swap to the safe interest rate and the expected likelihood of default. While such formulas are readily available, the calculations would require abstracting from risk aversion, liquidity premia and other market specific factors that could weigh on the arbitrage assumptions underlying such calculations. Apart from reservations of whether arbitrage conditions on financial markets hold as theory suggests, the close interdependence of the two unknown, namely the likelihood of default and the recovery value, casts doubts on the usefulness of such calculations. It would also be possible only for those corporations hat issued a bond or for whose debt there is a credit default swap.

The most granular source of information on recovery rates and recovery time is a study carried out by the European Banking Authority (EBA) in 2019/20. Prior to this exercise, the Commission had tasked an external contractor tasked to collect such data, but suspended the work in 2017 because it turned out that it was not feasible to obtain recovery rates at sufficient depth and representativeness. As follow up to this failed endeavour, the EBA carried out a benchmark study. It collected data from banks in the EU Member States on gross replacement rates, net replacement rates, i.e. after judicial costs, time for recovery and judicial costs. It performed three rounds of verification of data to ensure high quality and robustness of data.

The breakdown is consistent with that used by the World Bank, with the notable expectation of the recovery rate. The EBA term recovery rate is equivalent to the recovery value in the World Bank. The EBA recovery rate is the amount the bank recovered relative to the notional amount of the debt at the time of default, i.e. includes possible depreciation of the value but does not discount for the time of waiting. The gross recovery rate is derived from the amount before any deduction of any costs and the net

[221] First lien bonds.

recovery rate after deduction of costs. Numbers were collected for corporate credit, SME credit and also on other forms of credit that are less relevant for this impact assessment (i.e. commercial and residential real estate loans, credit cards, other consumer loans). 55 banks provided data on more than 4000 corporate loans and 105 banks on more than 150000 SME loans.

The table below shows the results for corporate credit, also demonstrating that the number of observations was low for many Member States and the bank populations not representative. The EBA exercise revealed that banks are using very different data standard to monitor loans defaults and recovery, which complicates the compilation of statistical data. The Commission is currently investigating with ECB and EBA possible ways forwards, including through the use of AnaCredit data.

Table A4.4: EU Benchmarks, Gross Recovery rate (%) per EU Member State - corporate

Country of the formal enforcement	Number of observations	Number of banks	Simple average	Weighted average	Standard deviation	1st quartile	Median	3rd quartile
AT	38	3	34.9	41.3	40	1.7	16	76.3
BE*	*Not shown	-	-	-	-	-	-	-
BG	252	3	67.9	53.6	39.3	23.6	97.1	100
CY	57	2	17.6	18	28.1	0	2	18.5
CZ	38	2	6.9	5	11.5	0	0	17.5
DE[1]	10	3	33.3	26.9	15.5	15	41.1	41.3
DK	17	3	95.2	97.7	11.3	99.1	100	100
EE	27	1	56.6	54.7	33.4	46.3	57.3	80.6
ES	332	6	42.2	54.6	43.8	0	25	100
FI	NA	-	-	-	-	-	-	-
FR	85	3	35.6	48.6	36.6	2.9	16.2	60.6
GR	353	2	10.9	10.7	28	0	0	0
HR	726	1	30.2	60	41.2	0	2.3	74.9
HU	NA	-	-	-	-	-	-	-
IE[2]	NA	-	-	-	-	-	-	-
IT	878	11	32.3	29.4	37.5	0	14.3	60.1
LT	NA	-	-	-	-	-	-	-
LU*	*Not shown	-	-	-	-	-	-	-
LV	NA	-	-	-	-	-	-	-
MT*	*Not shown	-	-	-	-	-	-	-
NL	180	2	67.5	42.9	35	49.5	70	100
PL	321	4	6.9	5	21.2	0	0	0
PT	403	5	35	21.1	41.2	0	8.4	82.3
RO	68	3	69.3	55.7	37.1	35.8	91.5	100
SE	14	3	92	100	20.5	100	100	100
SK	458	1	94.7	93.2	17.9	99.9	100	100
SK	14	2	28.6	24.8	40	0	3.1	28.2
EU27	**4,277**	**55**	**40.4**	**26.2**	**43.4**	**0**	**16.2**	**100**
NO	NA	-	-	-	-	-	-	-

Note: * not shown when the number of observations is below five. The EU27 include not shown observations.

[1] Based on a very low volume of observed data and, therefore, making generalisations about the whole banking sector can be misleading.

[2] Where non-judicial debt settlement (i.e., voluntary sale/surrender of property) are prominent features of workout in national financial systems distressed debt workout, judicial enforcement benchmarks will not reflect work out recovery rates, costs, or duration.

[3] For Corporate, SI shows a high number of loans with negative recovery amounts (46% of the total number of loans for the sample in the country). In case these loans were considered, the net recovery rate and gross recovery rate would be 50.4% and 50.8%, respectively.

Source: EBA (2020).

There is little information about the actual costs of insolvency procedures. Franks and Loranth (2014) in an analysis of bankruptcy cases in Hungary found that legal costs and fees accounted for 6 to 14% of the asset value on average. Costs are higher in going concern compared to immediate closures. This compares to 18% in the UK and 4.5% in Sweden, which however date back from sources in 2000 and 2005. The insolvency experts that populate the World Bank Doing Business index with their estimate of judicial costs produced numbers of 14.5% for Hungary and 10% for Sweden. Difference are due to different approaches and experiences. The table below reveals that the empirical study by Franks and Loranth builds on around 100 cases. The EBA collected data on judicial costs of loan enforcement from banks in its benchmark report (EBA 2020). The EU average was 2.1% of the outstanding value for corporate loans and 8.1% for SME loans. The EBA reported that foreign banks indicated higher judicial costs than domestic banks. When taken at face value, the average judicial costs for corporate loans are highest in Estonia, Romania and Bulgaria, those for SME loans in Greece, Portugal and France. The substantial difference that emerges in the country ranking when the weighted average instead of the simple average is taken suggests that the share of judicial costs is strongly determined by the magnitude of the underlying loan.

Table A4.5: Bankruptcy costs for Hungarian companies in Franks and Loranth (2014)

	(1) Immediate closure				(2) Going concern followed by liquidation				(3) Going concern followed by going-concern sale			
	N	Mean	Median	SD	N	Mean	Median	SD	N	Mean	Median	SD
Administration costs as a percentage of pre-filing assets	47	0.10	0.02	0.29	46	0.03	0.02	0.04	8	0.07	0.06	0.07
Liquidation costs as a percentage of pre-filing assets	47	0.26	0.13	0.39	46	0.27	0.12	0.56	8	0.23	0.13	0.25
Fees as a percentage of pre-filing assets	50	0.04	0.03	0.04	49	0.03	0.03	0.03	13	0.05	0.02	0.07
Direct costs as a percentage of pre-filing assets	47	0.42	0.25	0.61	45	0.36	0.22	0.57	8	0.37	0.30	0.31
Operating P/L as a percentage of pre-filing assets	–	–	–	–	47	−0.24	−0.18	0.43	10	−0.14	−0.20	0.87
Total costs as a percentage of pre-filing assets	47	0.42	0.25	0.63	44	0.53	0.46	0.45	8	0.50	0.51	1.10

Table A4.6: Judicial costs in EBA (2020, in % of nominal outstanding amount)

	Corporate loans			SME loans		
Country of the formal enforcement	Number of observations	Simple average	Weighted average	Number of observations	Simple average	Weighted average
AT	37	0.3	0.6	4,462	2.4	1
BE	NA	–	–	61	2.2	2.1
BG	245	6.7	4.6	2,617	11.3	5.9
CY	61	0.6	0.3	893	3.5	0.9
CZ	38	2.3	0.1	8,696	2	0.2
DE	–	–	–	925	2.3	1.3

DK	16	0	0	61	0.1	0.1
EE	24	21.2	0.5	14	1.5	0.7
ES	339	2.1	0.7	10,054	3.9	2
FI	NA	–	–	66	0.1	0
FR	11	0.1	0.1	1,480	13.5	2
EL*	*Not shown			387	19	7.1
HR	703	0.2	0	850	0.7	0
HU	NA	–	–	20,224	0.1	0.3
IE	NA	–	–	684	2.6	0.1
IT	1,088	1.1	0.2	18,863	1.7	0.7
LT	NA	–	–	371	0.4	0.1
LU	16	0.7	0.5	550	0.6	0.2
LV	NA	–	–	218	0.9	0.8
MT	35	4.9	2.3	60	5.1	2.1
NL	118	0.5	0	16,395	1.7	1.4
PL	331	0.4	0	14,938	0.3	0.1
PT	457	0.4	0.1	30,710	9	1.1
RO	61	13.8	13	7,701	2.4	5
SE	14	0	0	1,693	7.1	0.6
SI	830	0.6	0.6	5,381	0.7	0.6
SK	10	0.1	0.1	589	9.3	4.6
EU27	4,448	1.4	0.5	148,943	3.5	1.2

Source: EBA (2020)

2.3 Implications for the use of indicators in the analysis

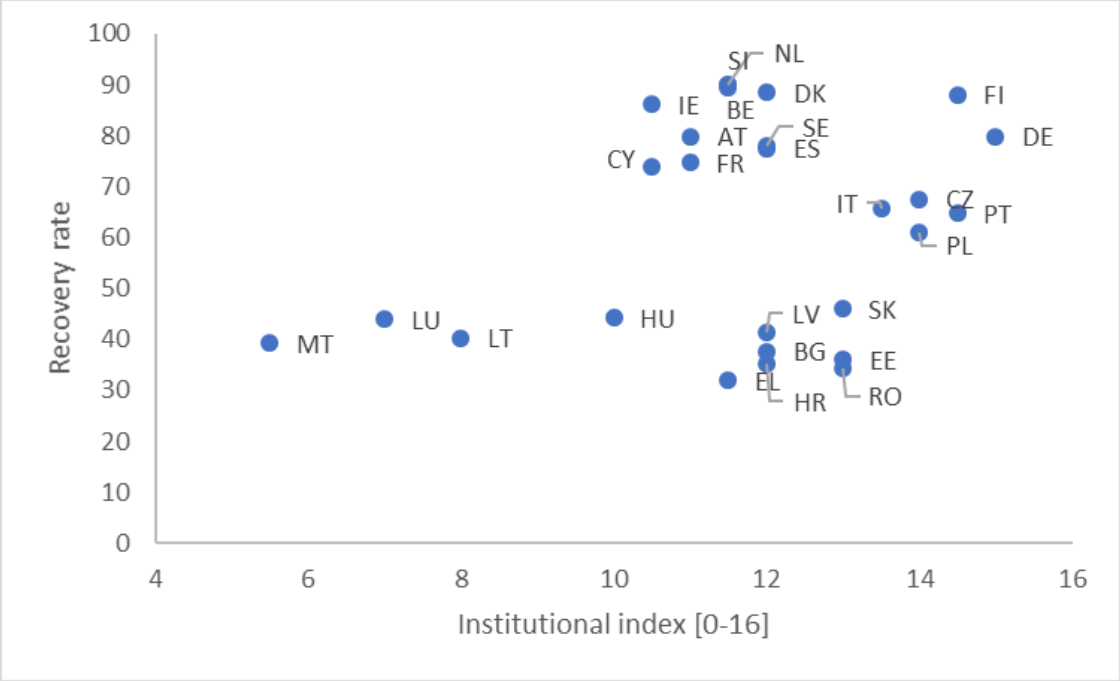
The information on recovery values, times and judicial information from the EBA benchmarking exercise is important input for the analysis. While they are not considered representative for many Member States, the EU aggregate should be sufficiently representative for scenario analysis at EU level. Its reliability is demonstrated by the findings in EBA (2020) of relationships between institutional features of insolvency regimes and the recovery rate of bank loans obtained from its benchmarking exercise. Its empirical analysis looked into the institutional variables from EC (2019) as determinants of recovery rates and recovery time, finding significant coefficients for several of the institutional variables, especially of collateral arrangements and creditor rankings.

Academic researchers used either the recovery rates or the institutional scores or the World Banks' aggregate of both in their studies. Given the good performance of the World Bank data in empirical research, their broad coverage and assuming that the reasons for their discontinuity are not found in observations for the EU Member States, the World Bank indicators are used in the analysis below that requires cross-country comparisons. Their shortcomings should however be duly noted.

The presence of best practices institutional features should have a positive impact on recovery rates. Since the World Bank Doing Business data includes also both input and output indicators, the chart below plots how they compare for the EU Member States in

2020. When expanded to all years and countries in the data set, there is a positive, but not high correlation between recovery rates and the "best practice" institutional approach, amounting to 0.22 for the EU Member States and 0.57 in all 211 countries covered.

Figure A4.10: Recovery rates and the strength of insolvency frameworks as measured through an institutional indicator, 2020



Note: The recovery rate is an indicator of the outcome of insolvency proceedings, the institutional index counts how many of 16 desirable features are present in a country's insolvency regime. See Table A4.3 for a breakdown of the desirable features in the World Bank doing business indicator used here.
Source: FISMA with World Bank doing business data.

Further statistical analysis with the World Bank data for the EU Member States 2012-2020 shows that the variation in the insolvency score explains only a small part of the cross-country differences in recovery rates. The R2 as measure of the share of variation explained by the estimate reported in the table below is very small in the simplest type of estimation. They become higher if GDP per capita is added as additional control variable (estimates 5 and 8).[222] If fixed effects are added (estimates 2-4 and 7), the R2 rises, but at the expense of declining coefficient and degree of significance of the insolvency index. This is not fully surprising since institutional parameters of insolvency regimes do not change a lot over time and are therefore similar to a country fixed effect. In most specifications, the coefficient ß is significant at the 5% level[223] and suggests that a 1

[222] A positive correlation between insolvency indicators and GDP or GDP growth is not uncommon in the literature. They appear in Djankov et al (2008), Smrncka (2015) and Becker and Ivashina (2021), albeit are interpreted as reverse causation. That is, richer countries are endowed with a better legal system, which also shows up in a more efficient treatment of corporate bankruptcies.
[223] The coefficient is significant provided that country-fixed effects are not used, which reflects that scores are relatively stable in Member States over time, i.e. are correlated with a fixed effect. Neither the coefficient nor the level of significance depends on whether GDP per capita is controlled for in the estimate or not.

point higher institutional score improves the recovery rate by 0.5-2.0%pts. This range can be used to translate changes to institutional scores caused by the policy options into changes to recovery rates.

Table A4.7: Regression results: insolvency outcome and institutional insolvency indicators

Recovery $rate_{ij}$ = Constant + ß * insolvency $index_{ij}$ + γ * GDP per $capita_{ij}$+ μ_{ij}								
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)
C	35.5	37.5	41.4	56.5	39.4	36.3	54.0	42.1
ß	2.1	1.9	1.5	0.2	1.4	2.2	0.6	1.3
SE of ß	0.41***	0.42***	0.29***	0.32*	0.41	0.55***	0.55	0.55***
γ					8.8E-6			8.5E-6
SE of γ					1.5E-6***			1.8E-6***
R2	0.05	0.07	0.87	0.89	0.13	0.06	0.93	0.14
period	2004-2020 (unbalanced)					2012-2020 (balanced)		
Fixed effects	none	time	country	Time and country	None	none	country	none
443 and 243 observations, respectively. EU Member States, * significant at 10% level, *** significant at 1% level; i, j per country i and year j.								

3. Numerical estimates of the impact of policy options on recovery rates and institutional insolvency indicators

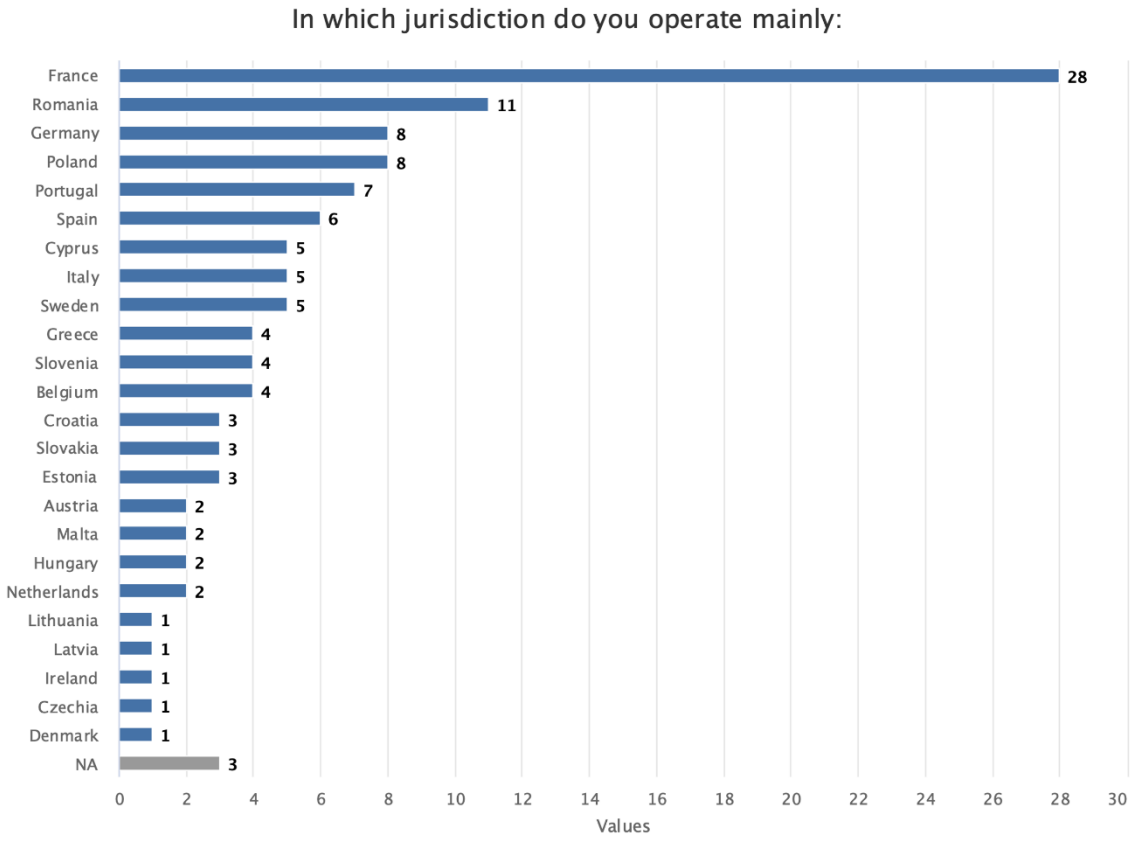
Quantitative analysis of how the introduction of the measures discussed in the impact assessment would improve insolvency indicators relies on a number of assumption. This section presents such analysis and the underlying assumptions. The first section uses the replies of the results of the Deloitte/Grimaldi survey with insolvency experts presented above and translates them into estimates about how targeted changes in insolvency regimes could translate into changes in recovery rates. The second section reviews maps how the targeted changes in insolvency regimes could improve the institutional insolvency indicators. This will be the basis to formulate scenario analysis of the different policy options. The value of these two sections will be apparent in the subsequent section, which reports estimates of what changes in either recovery rates or aggregate institutional insolvency indicators imply for monetary and economic variables.

3.1 Survey responses and recovery rates

A new data source is a survey carried out by Deloitte/Grimaldi in 2021/2022 for this impact assessment. Deloitte/Grimaldi has been tasked to gather insolvency experts' views on what targeted changes in insolvency regimes would mean for the efficiency of the insolvency regime, changes to the costs and changes to the recovery time. They asked 120 insolvency experts from 24 EU Member States about their assessment of the impact of harmonisation of targeted areas in insolvency rules on the determinants of the recovery rate, i.e. the time of recovery, costs involved or the recovery value. About 38% of the surveyed experts were legal experts and practitioners or insolvency lawyers, 24% regulated insolvency practitioners, 12% each judges in commercial courts or from financial institutions, 9% persons in public administrating handling insolvencies. The survey asked for estimates how introduction of rules at EU level across various elements would translate into changes in costs and time of cross-border insolvency cases. Experts

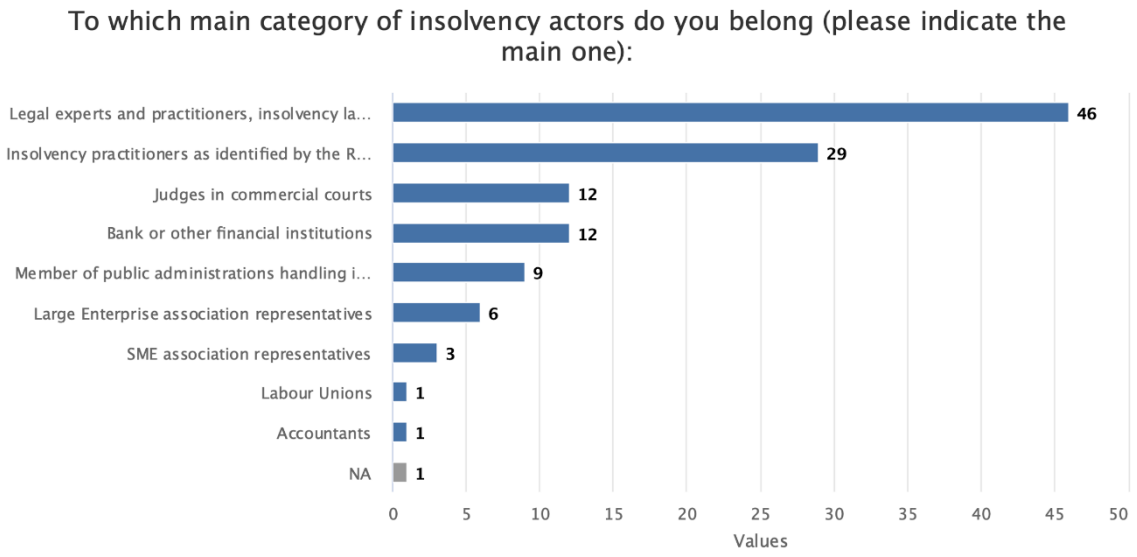
were also asked about their assessment of the efficiency of measures across the different elements.

Figure A4.11: geographical breakdown of respondents to the survey by Deloitte/Grimaldi (2022)



Source: Deloitte/Grimaldi (2022).

Figure A4.12: Breakdown by type of respondent in the survey by Deloitte/Grimaldi (2022)



Source: Deloitte/Grimaldi (2022).

Overall, the experts estimate that costs would fall by a double digit percentage points from measures in most areas. There is no area where more than 25% of the experts expect that costs would increase. The most optimistic 25% expects cost reductions of above 20% in most areas. Indications about time savings are highly correlated with those of cost reductions. In the absence of statistical data, reliance on expert views is common for all types of indicators in the area of insolvency. Their average assessment can be considered similar to a "market perspective" where each opinion might be biased but the aggregation of independent opinions forms an accurate description of the expected value. Although the experts did not receive guidance on how effective the measure will be, the context of a survey done on behalf of the Commission suggests that they assumed a fairly ambitious measure.

Table A4.8: Estimated change of costs from introduction of rules at EU level, distribution of indications from insolvency experts, in %

	Pre-packs	Avoidance actions	MSE	Asset tracing	Ranking of claims	Pari passu+	Directors' duties	Creditor committees
N/A	5.0%	1.7%	2.5%	5.0%	4.2%	3.3%	5.8%	#N/A
< - 40%	10.8%	7.5%	10.0%	10.8%	5.0%	2.5%	3.3%	#N/A
< - 30%	10.0%	8.3%	11.7%	19.2%	5.8%	6.7%	9.2%	#N/A
< - 20%	20.8%	18.3%	15.0%	14.2%	7.5%	3.3%	13.3%	#N/A
< - 10%	16.7%	23.3%	15.8%	15.8%	10.0%	12.5%	21.7%	#N/A
>-10 and < 10	20.8%	22.5%	31.7%	12.5%	46.7%	54.2%	36.7%	#N/A
> 10%	4.2%	7.5%	5.8%	5.0%	9.2%	6.7%	2.5%	#N/A
> 20%	6.7%	5.0%	3.3%	10.0%	8.3%	6.7%	5.0%	#N/A
> 30%	4.2%	4.2%	2.5%	5.8%	2.5%	3.3%	2.5%	#N/A
> 40%	0.8%	1.7%	1.7%	1.7%	0.8%	0.8%		#N/A
Average cost change*)	13.5	10.0	11.9	13.4	3.2	2.0	9.3	#N/A**
Average change in time in %								

	12.6	16.1	12.5	16.1	3.9	-0.6	9.4	1.4

+ At least pari passu treatment of certain unsecured creditors (tax authorities, employees etc.).

*) weighted average, used are mid-ranges for each interval. + and -50 for the greater 40 indications.

**) the survey asked only for the reduction in time yielded by harmonisation of rules on creditors' committees. The average of replies was minus 1.4%.

Since the survey specified numerical ranges for the latter two determinants of recovery rates, it is possible to transform the experts' replies into quantitative estimates of the impact of the targeted changes on recovery rates. The table below reports the results transformed into the median (50%), lowest and highest quarter (25%). Since expert were asked to indicate a range, the centre of each range was used to calculate the average.[224]

Table A4.9: Summary indications of insolvency experts in the Deloitte/Grimaldi survey

	Pre-pack	Avoidance actions	MSE	Asset tracing	Ranking of secured claims	Pari passu	Directors' duties	Creditors' committes
Cost reductions								
Approval rate	58.3%	57.4%	52.5%	60.0%	28.3%	25.0%	47.5%	NA
average	13.5	10.0	11.9	13.4	3.2	9.3		NA
median	10-20	10-20	10-20	10-20	-10 - +10	-10 - +10	-10 - +10	NA
Time savings								
Approval rate	67.5%	54.1%	52.6%	65.1%	32.5%	15.8%	46.7%	37.5%
average	12.6	16.1	12.5	16.1	3.9	-0.6	9.4	1.4
median	20-30	-10 - +10	10-20	10-20	-10 - +10	-10 - +10	-10 - +10	-10 - +10

The approval rate is the share of insolvency experts that indicated that the measure will lead to a reduction in costs and time, respectively.

The subsequent table uses the average reduction in judicial costs and time from the Deloitte/Grimaldi survey and combines it with the simple averages for corporate loans in the EU from the EBA study about recovery values, recovery time and judicial costs (40.4, 3.4 and 1.4%, respectively), and the ECB cost of borrowing to non-financial corporations of 1.36% in December 2021. When using this information to calculate the recovery rate, the introduction of an MSE insolvency regime would increase the recovery rate from 37.2 to 37.7%. The impact of other measures on the recovery rate is in a similar ballpark. The extent of the decline depends on the starting assumption. If the weighted average instead of the simple average from the EBA study is taken, the impact would decline by about 1.25% on average, and if the median is taken by 0.4%. This reflects that small loans have a lower recovery value and higher judicial costs.

[224] French respondents are overrepresented in the sample. They were underrepresented in the interim version of the report, which reported answers from 44 respondents. Averages have remained broadly stable from the interim to the final report, suggesting that the French overrepresentation has no marked effect on the average. Exceptions were limited to indications on the time of recovery, where the final sample was much more optimistic on the time savings from transaction avoidance and less optimistic on the time savings from pre-packs and creditor committees.

Table A4.10: Estimated increase in the recovery rate from the introduction of rules at EU level

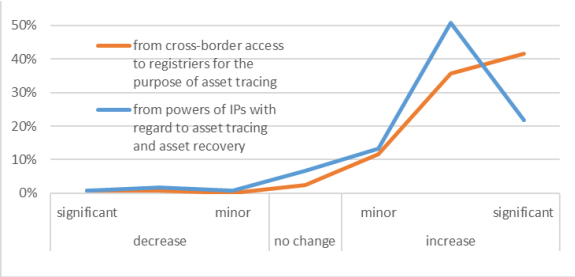
	Asset recovery	Procedural efficiency	Distribution of assets	Sum
		Option 2		
Costs in %	-39	-12	-3	-49
Time in %	-44	-13	-5	-54
recovery rate (%pts)	1.56	0.38	0.13	2.07
		Option 1		
Costs in %	-28	-12	0	-36
Time in %	-31	-13	-1	-40
recovery rate (%pts)	1.02	0.38	0.02	1.42

Note: Assumptions are a recovery value of 40.4%, recovery time 3.4 years, judicial costs 1.4%, interest rate 1.36%. Changes in costs and time as average indicated by insolvency experts in the previous table. It is furthermore assumed that the measure on transaction avoidance under option 1 yields 2/3 of the effect as in option 2, that of cross-border asset tracing 1/3, that on directors' duties 2/3.The aggregate effect (sum) is calculated as the product of the individual effects.

Insolvency experts were not asked how the measure will be implemented. They may have assumed that the measures they were interviewed about would be transformed in the most effective manner. Hence, their estimates could be read as the expected outcome of the most ambitious policy option. Regarding the options on pre-packs, MSEs, ranking of secured claims and creditor committees, the policy options are ambitious and therefore their indications were taken as basis for the estimate of the impact of their realisation on the recovery rate. On avoidance actions, it is conceivable that more elements than suggested could be harmonised and that in particular the opportunities to seize assets carries a potential to increase recovery values. The replies by insolvency experts in Deloitte Grimaldi on the questions of asset tracing and Since the measure includes the core elements, an estimate that the measure yields 2/3 of the indicated effect seems conservative. Since cross-border asset tracing is a preparation to asset seizure, it is assumed that the effectiveness of asset tracing without asset seizure in option 1 yields only 1/3 of the effect. Regarding directors' duties, option 2 is encompassing, while the absence of a change in the direction of their interest from shareholders to creditors should lead to a discount. It is assumed that the obligation to file for insolvency accounts for 2/3 of the impact on the recovery rate.

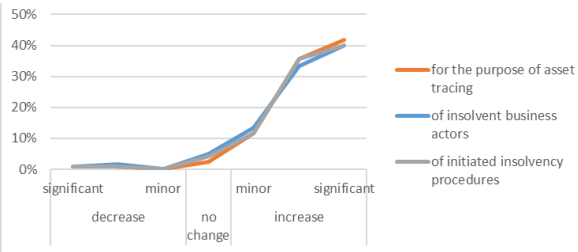
The survey asked for an assessment of the effectiveness of various means to facilitate the treatment of cross-border asset recovery. More insolvency experts expect a significant increase in efficiency from the cross-border access to registries for asset tracing than from more powers for IPs to trace and recover assets. While fewer experts expect a significant increase from asset tracing and asset recovery than from the cross-border access to registries for the purpose of asset tracing, overall 70% expect a more than minor increase in the efficiency from the latter. Regarding better cross-border access to different kinds of registers, for asset tracing, of business actors, and of initiated insolvency procedures, experts' assessments are very similar. More than 75% expect a more than minor increase in efficiency.

Figure A4.13: Share of insolvency experts expecting a change in the efficiency in cross-border insolvency cases



Source: FISMA with Deloitte survey data.

Figure A4.14: Share of insolvency experts expecting a change in the efficiency in cross-border insolvency cases from acces to registries



Source: FISMA with Deloitte survey data.

The insolvency experts were not asked about cost and time savings of the transparency enhancing measures. These measures can also not be expected to lead to a direct reduction in time and costs, but to the already impossible to measure information and learning costs. The insolvency experts were however asked about the impact on the effectiveness on cross-border investors of certain types of transparency enhancing measures. Their assessment of the effectiveness is comparable to that of the other measures. For example, they rated a glossary of insolvency terms as efficient as common rules on the treatment of senior creditors and a standard ontology as comparable to the pre-pack.

Table A4.11: Assessment of insolvency experts of measures to increase the increase transparency in insolvency cases for foreign creditors (distribution of views).

Impact on the effectiveness for the creditor	Development of a glossary of insolvency terms and of the equivalent professional figures in different jurisdictions to aid translation of claims filing.	Standard ontologies (A set of concepts and categories in the insolvency subject area and domain showing their properties and the relations between them)	Standardised models for filing claims	Insolvency-dedicated automated translation tools for documents, inscriptions into registries, insolvency proceedings	Authentication and validation of claimants to ensure legitimacy of access and claims filing
Decrease	0.0%	0.0%	2.4%	0.0%	0.0%
No change	9.5%	22%	7.1%	9.3%	9.8%
Minor increase	26.2%	24.40%	26.2%	25.6%	29.3%
Increase	38.1%	41.50%	38.1%	44.2%	39%
Significant increase	26.2%	12.20%	26.2%	20.9%	22%
Score	1.06	0.88	1.07	1.07	0.99

Note: The score is calculated by weighing "no change with 0, an increase with 1, a minor increase with 0.5 and a significant increase with 2 and likewise for negative values.

Source: Deloitte/Grimaldi 2022 and FISMA calculations.

Table A4.12: Assessment of insolvency experts of measures to increase the efficiency in insolvency cases for foreign creditors (distribution of views).

Impact on the effectiveness for the creditor	pre-pack	avoidance actions	MSE	Ranking of senior creditors	creditor committee
Significant	2.4%	2.3%	4.7%		4.8%

decrease					
Decrease	2.4%	4.5%	2.3%		4.8%
No change			11.6%		
Minor increase	21.4%	11.4%	27.9%	7.1%	33.3%
Increase	23.8%	36.4%	20.9%	23.8%	26.2%
Significant increase	33.3%	34.1%	25.6%	47.6%	28.6%
Score*	0.62	0.78	0.47	0.99	0.33

*) The score is defined as 0 indicating no efficiency gains, 0.5 marginal gains, 1 gains and 2 significant gains and likewise for negative values. It is calculated by multiplying the % shares with these weights.

3.2 Changes to aggregate insolvency indicators

This section derives estimates of the impact of the various policy options on institutional indicators of insolvency regimes. This served as robustness check of the validity of the survey responses. It also adds information on those policy options that were not covered in the Deloitte/Grimaldi survey. A third motivation for this step is that some academic studies use these institutional indicators as input for their empirical analysis of insolvency regimes on economic variables. Simulating what the policy options would mean for the institutional indicators would therefore allow using the results of these studies in the subsequent section.

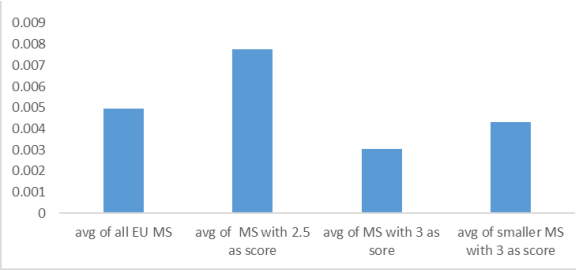
Insolvency triggers

While the consequences of an insolvency trigger should be positive for the recovery time and the recovery value, there are no means to quantify the effect. The specification of the insolvency trigger is covered through three features in the World Bank Doing Business insolvency indicator. Convergence to the best practices would lift the insolvency index by 0.5 in the 14 Member States that have not yet reached the maximum. This would yield a 3% point improvement in their overall insolvency score.

The following charts shows an experiment of how the information from the institutional indicators can be used. It seems plausible to assume that foreign investors will prefer to invest in countries with a similar insolvency regime everything else equal. The more geographical dispersed their investment is, the more do investors face variations in insolvency regimes, suggesting that investment into Member States should be more clustered the more different and inefficient their procedures. A measure of clustering is the Herfindal-Hirschleifer index of market concentration applied on intra EU portfolio investment flows. The left hand chart shows that intra-area portfolio investment is much more concentrated in countries that score 2.5 in the World Bank sub-indicator of commencement of proceedings, compared to those that score 3. The comparison of the concentration[225] measure with the best practices in an EC sub-index of commencement of procedures in the right hand chart below yields a less conclusive picture.

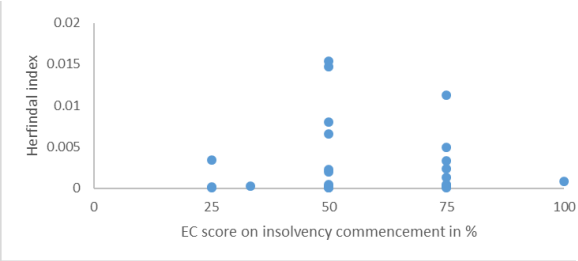
[225] A Hirschleifer-Herfindal index over the market share of 83 countries' portfolio debt investment in the EU Member States was calculated with FinFlow data for 2020 from the EC Joint Research Centre.

Figure A4.15: Intra-EU concentration of capital flows (Herfindal index versus World bank subindex of commencement of procedures)



Source: FISMA with World Bank and JRC data.

Figure A4.16: Intra-EU concentraton of capital flows (Herfindal index versus EC 2019 sub-indicator on commencement of procedures)



Source: FISMA with Steffek (2019) and JRC data.

Creditor committees and ranking of claims

Representation in creditor committees is more costly for foreign investors and bargaining with other foreign creditors more difficult for them. The empirical estimates in the economic literature about the impact of insolvency rules on recovery rates and domestic financing costs[226] therefore look equally important for foreign investors and may represent a lower bound for them.

The introduction of effective creditor committees would lift the World Bank's institutional indicators of insolvency. The World Bank indicator defines four conditions for creditor participation and allocates one score for each of these conditions, which means that the fulfilment of an extra condition increases the insolvency-strength score by 6%.[227] Only one Member State was awarded the full score of 4 out of 4 in 2020 for the creditor participation index. Applying the coefficient from the relationship between the recovery rate and institutional features shown in the estimates above, implementation of one additional feature would increase the recovery rate by between 2.5 and 3.5 percentage points. This compares to the 1.7 percentage points from the scenario results based on the Deloitte/Grimaldi Survey.

The OECD insolvency indicator would rises if creditor participation became more effective and a regime for MSEs were introduced. Regarding creditor participation, the OECD indicator increases by 1 score, representing an increase by 7.5%, if dissenting investors cannot be crammed down. Only 1 Member State received this score and several others were attributed half the score for the case that creditors can be crammed down in a restructuring, but the dissenting creditors do not receive more than in a liquidation case. Introduction of special procedures for SMEs would improve the aggregate OECD

[226] See for example IMF (2019), AFME (2016) and the literature reviewed in Kliatskova and Savatier (2020).

[227] These are " (i) whether creditors appoint the insolvency representative or approve, ratify or reject the appointment of the insolvency representative; (ii) Whether creditors are required to approve the sale of substantial assets of the debtor in the course of insolvency proceedings; (iii) Whether an individual creditor has the right to access financial information about the debtor during insolvency proceedings; and (iv) Whether an individual creditor can object to a decision of the court or of the insolvency representative to approve or reject claims against the debtor brought by the creditor itself and by other creditors."

insolvency by 7.5%pts, which the OECD indicated as missing in 8 Member States. This might give an idea on the importance of procedures for MSEs.

The estimates in EBA reveal that both the ranking of claims and creditor committees have a significant impact on recovery rates. When taken at face value, the estimates suggest that the absence of preferential treatment is associated with a 1.5% higher recovery value and a 1.3% shorter time to recovery. The size of the coefficients is independent from whether the public sector or employees as preferred creditor group is looked at. The EBA (2020) estimates suggest that the possibility for creditors to influence the proceedings through creditor committees increases the recovery value of corporate loans by 6 %pts and reduce the time to recovery by 2.5%. This is a much higher impact than what the insolvency experts interviewed by Deloitte/Grimaldi indicated.

Judicial capacity

Differences in Member States' judicial capacity may be the reason why there is no stronger relationship between institutional indicators of insolvency as "input to the insolvency process" and the recovery rates as outcome of the insolvency proceedings as shown in figure A4.10 and Table A.4.6 above. The strong contribution of country-fixed effects in Table A4.6 underpints the notion that judicial capacity could play indeed a role.[228]

An analysis of judicial capacity in the context of insolvency proceedings is useful for two reasons.

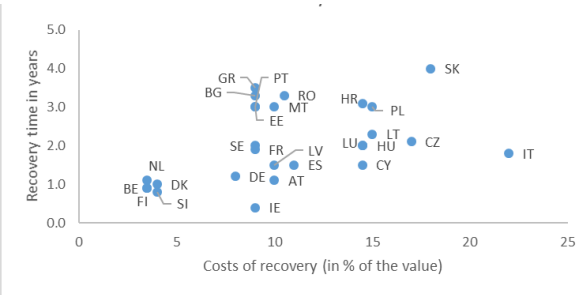
- First, by demonstrating that constrained judicial capacity is a source of low recovery rates, it could establish a motivation for Member States to improve non-legal framework conditions. Measures in the competence of Member States, that they undertake individually, could, for example, relate to setting up specialised courts (or court chambers), dedicated exclusively to insolvency proceedings, or better training of insolvency judges. In addition, there could also be additional measures that Member States can take building on recent EU law setting out rules for insolvency practitioners (e.g. on conflict of interest).
- Second, the analysis of judicial capacity can sheds a light on the indirect effects of legal changes to insolvency proceedings on the capacity of courts to deal with them. Some measures discussed in this impact assessment would directly improve the efficiency and effectiveness of national judicial systems in dealing with insolvency proceedings. For example, an earlier start of proceedings (due to enhanced duties for directors to file for insolvency) as well as better means to avoid asset misuse, and better means to trace the already misused assets, should facilitate (and expedite) the work of courts and insolvency practitioners. The introduction of an MSE regime may lead to a higher workload of courts and whereas it is not possible to quantify any of the cost savings stemming from the measure, it can be reasonably assumed that they will outweigh at least partly (if not entirely) the costs of the new MSE regime.

[228] See the high R2s in columns 3, 4 and 7 compared to those in columns without country-fixed effects.

There is little literature on the effect on judicial capacity on the outcome of insolvency procedures.

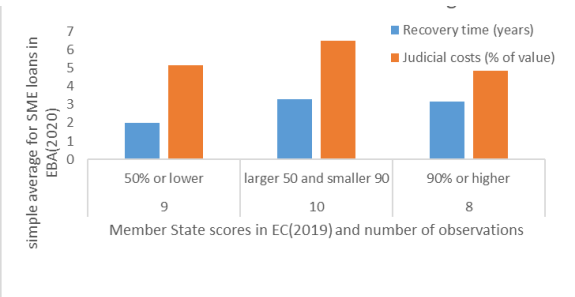
- Iverson (2018) carried out ann empirical analysis on how judicial capacity impacts on recovery rates and the likelihood of whether companies are restructured or liquidated case load with US data. He found restructuring more frequent and that the recovery value was significantly lower in busier courts.
- EC (2019) retrieved information about judicial capacity through four questions of which two were numerical: The court cases per capita, the ratio of incoming over resolved cases, whether there are specialised courts for insolvency cases and whether it is possible to communicate electronically with courts and insolvency administrators. Many Member States did not give indications on the numerical questions. Those that did said that the clearance rate was close to 90%. 20 Member States indicated there were courts specialised in insolvency cases.
- EBA (2020) did not report court capacity a significant determinant of recovery rates or time.
- The left-hand chart below suggests a weak positive correlation between judicial costs and recovery time. The right-hand chart below reveals that the notion of a linear positive relationship between judicial costs and judicial capacity does not appear when numbers from the EC benchmarking exercise are used instead of the

Figure A4.17: Recovery time and legal costs in the World Bank insolvency indicators, 2020



Source: FISMA with World Bank Doing Business data.

Figure A4.18: Judical capacity and recovery performance for SME loans in the EC insolvency benchmarking exercise



Source: FISMA with data from EBA (2020) and Steffek (2019).

The number of about 150,000 corporate insolvency cases per annum in Table A4.1 compares to about 40 million cases brought to court in the EU Member States each year, i.e. less than 0.4%.[229] This low aggregate number hides substantial differences across Member States. Using the ratio of both, the proportion of insolvency cases is on average 1.4% across the EU Member States. There are two Member States where the proportion is much higher: Cyprus at about 12% and Luxembourg at 9%. Both Member States are known to the the domicile to numerous holding companies, often of multinational

[229] 40 million court cases is a broad approximation based on the numbers of criminal, civil, commercial, administrative and other cases reported to Eurostat. Not all Member States report and data is not complete over time and types of court cases. It covers only first instances. A second data source is the EC Justice Scoreboard, which builds on data delivered by Member States to CEPEJ (2022). It does not cover criminal cases, lacks some Member States and shows different data than Eurostat for some Member States.

character, which may be wound up more often than other enterprises.[230] The average of the EU Member States without those two would be 1.1%.

Insolvency cases seem to last much longer and therefore be costlier than other cases. Although direct data on the costs or length of corporate insolvency cases is not available, the EBA data on the time to recovery indicates an average length of about 3 years across EU Member States, the World Bank recovery time is about 2.5 years among those EU Member States where the data is derived for the case of a wound up corporation.[231] This compares to an average of 0.71 years in the time to resolve a non-criminal in the first instance according to the EC Justice Scorebard.[232] The EC Justice Scoreboard even reports numbers for the length of insolvency cases for a number of Member States. These data, however, refer to total insolvency cases, i.e. personal and corporate. The average was 514 days in 2020 in the reporting 18 Member States.[233] This disposition time was longest in Malta (3407 days), Czechia (1460) and Spain (1187). If one accepts the length of proceedings as an indicator for the cost of a judicial process, insolvency procedures are about two times more expensive than other non-criminal court procedures.

As second metric for the efficiency of a judicial system, CEPEJ (2022) uses clearance rates as the ratio between closed and incoming cases. This metric is available for non-criminal cases and – for a limited subset of Member States – for insolvency cases. It shows that the average clearance rate of insolvency cases across the EU Member States was 108.6% in 2020, up from 105.3% in 2019.[234] The clearance rates were close to or above 100% in most Member States in 2020, with the exceptions of Bulgaria (89.2%) Malta (42.9%) and Spain (78.9%). These three Member States had also higher than average judicial costs in EBA 2020 (see Table above). Overall, the magnitude of judicial costs and time to recovery appear related. More efficient organisation of judicial processes could bring down both and seem to be particularly valulabe for those few Member States with low clearance rate to reduce their backlog.

The table below summarises these different indicators of judicial efficiency at Member State level in order to identify where judicial systems are more stretched in general, more stretched from insolvency cases in particular and where therefore changes to corporate insolvency regimes may led to bottlenecks. The colour code signals that an indicator is below a certain threshold considered as warranted, i.e. a clearance rate below 100% means the court system was not able to cope with the incoming cases in a year and a more than average disposition time unveils that cases take longer than in other Member States. The indicators stem from the EC JUST scoreboard and the CEPEJ (2022) study

[230] The Luxembourgish statistics show that holding companies and fonds account for about 30% of the corporate insolvency cases.
[231] These were BG, EE, EL, HR, LV, LT, LU, HU and RO.
[232] There is no natural benchmark for the length of a court process at EU level. There is no 2019 data for six Member States, including DE. The length varies between 19 days in DK and 882 days in CY. The number of 0.71 years (equal 260 days) was derived as the population weighted average of all Member States that reported data for 2019. The simple average was 175 days. The weighted average is higher because the two largest Member States in the panel had above-average disposition times Data for 2020 are higher, due to the Covid crisis.
[233] See CEPEJ (2022), Table 3.5.1. The 382 days disposition time for insolvency cases compares to 365 for employment dismissal cases and 188 for litigious divorce cases in 2019.
[234] Not all Member States contributed data.

underpinning it. Since the CEPEJ study documents wide differences in how numbers are reported, the cross-country comparision needs to be treated with caution. It provides an illustration and starting point for more detailed research. Obervations are missing for some Member States (DE, EL, PT) The Covid crisis may furthermore distort the information from the 2020 observations, which are the most recent available to date. That said, the simple benchmarking exercise undertaken with the table below already suggests numerous valuable insights.

Markedly low clearance rates in Cyprus, Ireland and Spain suggest that the general court system faces a tighter work load relative to other EU Member States. In most Member States the clearance rate was above 100% in 2020 or slightly below. In some of them, however, the rate decline relative to one below 100 in the year before, suggesting a rising backlog: France, Malta, the Netherlands. In Cyprus, France, and Malta, the low clearance rate coincides with a longer duration of court cases.

The clearance rate of insolvency cases was on higher average than for other non-criminal cases. In Ireland and Spain it was still very low in line with the hypothesis of tight court capacity in general. While there is no data for Cyprus, the very high recovery time for corporate and SME loans in the EBA benchmarking exercise suggest the situation is similar in that Member State. The clearance rate for insolvency proceedings was also low in Belgium, Bulgaria and Malta, whereas the low rate in Hungary in 2019 contrasts with a very high rate in 2020.[235] The low insolvency clearance rate in Malta is consistent with longer duration of insolvency proceedings. The indications are less clear cut for Belgium and Bulgaria.

Based on these two metrics, Cyprus, Ireland, Spain and Malta were identified as the Member States that would potentially be the most exposed to a possible negative consequence from the MSE regime on their respective court capacity. Spain has, however, just introduced a special shortened insolvency procedure for micro-companies which is already available also for microcompanies with no assets. The EU MSE regime is therefore unlikely to lead to a further significant impact (beyond that from the implementation of the national regime) on their judicial capacity.

[235] The absolute number of Hungarian insolvency cases reported in CEPEJ (2022) is much lower than the number of corporate insolvency cases in Hungarian statistical office.

Table A4.13 Metrics of judicial capacity to deal with insolvency cases in the EU Member States

	Non-criminal cases				Insolvency cases				Time to Recovery	
	Clearance rate		Disposition time		Clearance rate		Disposition time		Corp.	SME
	2019	2020	2019	2020	2019	2020	2019	2020	2019	2019
AT	100.4	99.7	58.6	63.2	100.5	120.4	144	149	1278	840
BE	100.8	98.1			NA	29	NA	NA	NA	1059
BG	99.1	100.9	93.2	107.5	100.2	89.2	237	281	1497	1424
HR	92.8	103.6	130.3	119.5	131.2	141.5	276	328	876	110
CY	97.9	88.3	882.4	1086.7	NA	NA	NA	NA	803	1497
CZ	100.8	98.2	157.5	170.4	104	103.2	1201	1460	1862	1570
DK	100.6	100.8	18.8	17.3	99.9	128.1	345	296	621	1095
EE	100.0	101.3	31.5	24.8	98.7	97.3	96	54	402	730
FI	94.8	105.1	105.3	97.5	98.7	121.6	253	198	913	511
FR	99.4	93.6	387.8	554.4	105.6	147.5	NA	NA	1825	1351
DE	NA	NA	NA	NA	NA	NA	NA	NA	*2117*	*621*
EL	NA	NA	NA	NA	NA	NA	NA	NA	475	548
HU	100.7	98.3	69.2	80.5	84.6	147.6	112	8	NA	657
IE	75.4	62.0	NA	NA	84.1	105	NA	NA	*2373*	*2227*
IT	103.3	102.6	367.2	471.5	101.4	101.2	111	143	1935	2336
LV	100.0	99.0	25.4	27.8	121.3	141.5	573	502	NA	803
LT	101.2	96.7	51.5	67.8	120.5	140.9	262	255	NA	1168
LU	92.6	95.2	NA	158.2	100	100	NA	NA	511	694
MT	91.3	90.9	343.9	413.5	121.4	42.9	1031	3407	2081	1935
NL	99.6	98.5	79.7	91.0	NA	NA	NA	NA	511	657
PL	90.2	104.3	111.2	109.9	94.6	99	130	105	73	438
PT	NA	NA	NA	NA	101.2	99.2	47	59	1132	1205
RO	100.2	96.7	151.7	185.5	115	112.8	331	399	1424	1387
SK	91.1	113.0	134.9	86.8	101.6	103.4	33	36	1387	913
SI	101.8	98.9	55.9	69.4	140.7	138.1	545	589	2555	1460
ES	93.6	89.8	274.3	348.8	86.1	78.9	1146	1187	840	1205
SE	100.4	102.2	138.4	123.3	NA	109.7	NA	305	657	219
AVG	97.0	97.4	174.7	203.4	105.3	108.6	381.8	513.7	1132	1132
BM	100	101	174.7	203.4	105.3	108.6	381.8	513.7	1132	1132
CBM	90	90	350.0	406.9	210.6	217.2	763.7	1027.5	2263	2263

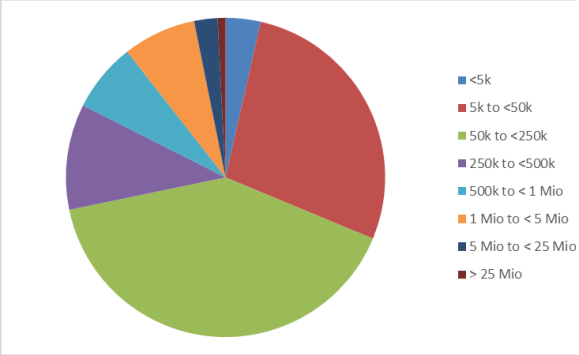
Data in italics and smaller font considered not representative (DE and IE), insolvency cases cover corporate and personal insolvency, the recovery time relates to corporate (corp.) and SME loans. Clearance rate in % (concluded to incoming cases), disposition time and time to recovery in days, AVG = average, BM = benchmark (100% or average), CBM critical benchmark (90% or two times average). Observations weaker than benchmark in yellow and if weaker than critical benchmark in red.

Source: CEPEJ (2022) for non-criminal and insolvency cases, EBA (2020) for time to recovery

Nevertheless, it needs to be stressed that the heterogeneity of court systems across Member States and the existence idiosyncratic factors prevent strong conclusions from the exercise above. Two idiosynractic factors are worth highlighting.

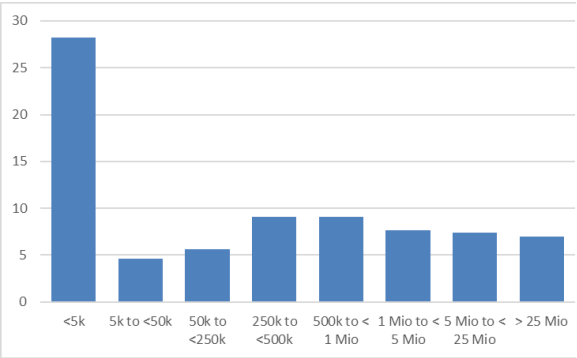
First, some Member States do not open an insolvency proceeding if the available assets are lower than the cost of the proceedings. This practice reduces judicial burden. Respondents to the public consultation pointed at Belgium, Germany, Spain, Greece and Italy and Austria as examples. While there is no encompassing data overview, the German data demonstrate the magnitude of this phenomenon: The German statistical office published detailed data about the distribution of insolvency cases across corporates in 2021, revealing inter alia that the majority of cases concern assets worth EUR 50,000 to 250, 000, followed by those in the range 5000 to 50,000. The average claim per case was EUR 3.5 million in that year. Almost 30% of the insolvency applications were rejected, most often for those with claims below EUR 5,000. Between 5 and 10% of the applications were rejected even for claims above EUR 250,000.[236]

Figure A4.19: Distribution of corporate insolvency applications in dependence of predicted claims in Germany 2021



Source: FISMA calculations with Destatis data.

Figure A4.20: Share of rejected corporate insolvency applications in dependence of predicted claims in Germany 2021, in %



Source: FISMA calculations with Destatis data.

Second, Member States may have different approaches how they allocate court capacity to different types of cases. Societal preferences, political and economic needs may have an impact. France introduced a special simplified insolvency procedure for MSEs in 2019. The coincidence of a low clearance rate for non-criminal cases and a high one for insolvenc cases may reflect that France allocated more court capacity to deal with insolvency cases to make the new MSE regime work. The profound improvements in the insolvency clearance rates in Hungary and Ireland between 2019 and 2020 may also be caused by a reallocation of resources to insolvency cases, albeit it is also possible that lower insolvenc cases during the Covid crisis contributed too. Apart from these two Member States and France, a strong increase in insolvency clearing rates, coinciding with a weakening of total clearance rate can be observed for Austria, Latvia and Lithuania.

MSE loans

Mirco and small firms are the backbone of the EU economy. The available data suggests they face two adverse effects. First, outcomes from insolvency proceedings tend to be poorer for smaller than for larger corporations. Second, in the Member States that practice the rejection of credit applications because the costs for the judicial outweigh the estimated revenues, small firms are more likely to find their application rejected. The

[236] The share of rejected applications was even higher at 32% in Austria in 2021 according to KSV1870 (2022). The average expected claim of all applications was EUR 540,000 in 2021 and 1 million in 2020.

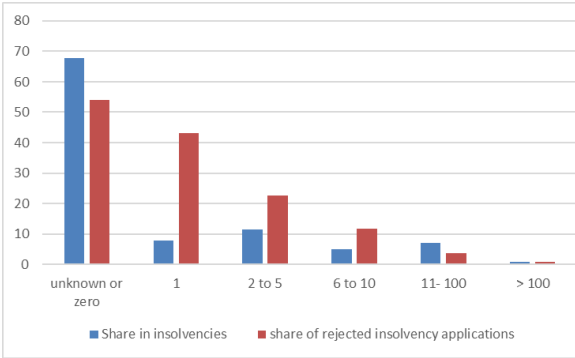
benchmarking study by EBA (2020) documents evidence of the first effect: Non-performing SME loans were more frequent than corporate loans in. Banks reported more than 150,000 SME loans and 4500 corporate loans that were non-performing. The study found that the benchmark recovery value of SME loans was about 5 percentage points lower than that of corporate loans for the EU average, but higher in 7 of the 18 Member States for which both numbers could be established.The recovery time was broadly similar, with shorter time in 15 out of 26 Member States. Since the wind-down of a larger corporate than of a micro enterprise is more complex, one would expect that it takes longer. A longer recovery time for SME than for corporate loans could therefore indicate efficiency potentials from simpler procedures for small firms. Among the Member States for which this is the case are Member States with tight court capacity: Cyprus and Spain. Also Italy, Portugal and Luxembourg could have such efficiency potential. Judicial costs – measured in % of the recover value are 2.5 times higher for SME loans than for corporate loans (1.4 vs 3.5%) in relative terms for the EU aggregate, but not in all Member States.

The previous section already presented the issue that corporations find their application for insolvency rejected, which leads their creditors to retract to individual enforcement procedures and increases the uncertainty for the debtor when he will be granted a second chance. Germany and the France follow different practices and both publish granular data to allow for a comparision.

- In Germany, corporations with up to 10 employees accounted for 87.8% of all firms, 92% of the insolvency applications and 31% of the rejected credit applications. In total numbers: 4036 micro firms found their credit application rejected in 2021, out of a total of 9500 total corporate insolvency applications. The smaller the firm, the higher the ratio of rejection.
- France introduced a new insolvency regime for MSEs in May 2019. A standard winding-up procedure lasts on average 2 and a half years while the simplified court-supervised winding-up procedure should lasts overall 1 year.[237] Micro firms amount for 96% of the firm population and 94% of the insolvency cases. Their share in total insolvency cases did not increase with the introduction of an MSE regime, the slight decline since then started in the months before the Covid crisis and accelerated during this crisis. In the months up to the end-2019, the share of insolvent firms relative to exiting firms also declined. One could have expected that access to a simpler insolvency regime could increase this share.
- Data is patchy for other Member States. Greece introduced an MSE regime in June 2021. There is not data yet to monitor the effect. 79% of the insolvent firms had fewer than 10 employees in Spain 2018-2020. In Austria, 32% of credit applications were rejected in 2021.[238]

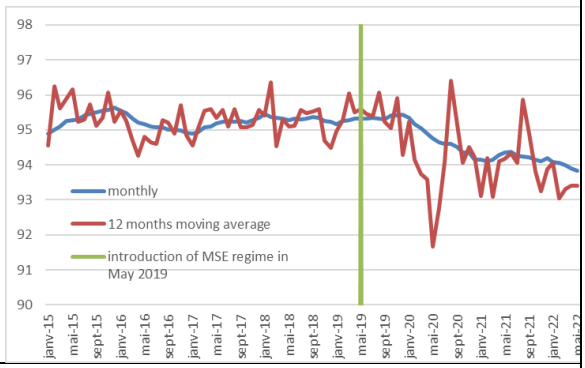
[237] The completion of a simplified procedure takes between 6 to 9 months for a MSE with a single employee and a net turnover of less than or equal to EUR 300 000.
[238] See KSV1870 (2022).

Figure A4.21: Corporate insolvencies in Germany by number of employees, 2021



Source: FISMA calculations with Destatis data

Figure A4.22: Share of corporate insolvencies of micro firms (less than 10 employees) in France



Source: FISMA calculations with Banque de France data

Granting all insolvent corporations access to insolvency proceedings could pressurise judicial capacity since the recovered assets would in many cases not be sufficient to cover the judicial costs. Any quantification of the effect would rely on strong assumptions and the combination of data from different sources. the best that can be done is to be transparent on the data and assumptions.

- One of the assumptions can be derived from the indications of insolvency experts in the survey by Deloitte/Grimaldi (2022). They point to time respectively cost savings of about 12% from the introduction of an MSE regime. This is still substantially below the shortening that the French MSE regime aims for, i.e. from 2 to 1 year.
- The EBA (2020) benchmarking exercise revealed judicial costs of 3.5% of SME's nominal amount of outstanding debt.
- The EBA does not report the outstanding debt of SMEs and the average amount of insolvency cases in Germany of EUR 3.5 million looks not representative for small firms. Eurostat's national accounts show that the total about of NFC debt liabilities in the EU is EUR 18324 billion.[239] A possibility to estimate the share of small firms consists in using the 12% share that small coporate loans (< EUR 250k) represent in total bank loans to NFC in the euro area according to the ECB MIR statistics. MSEs could therefore have outstanding debt of EUR 2200 billion.
- According to the scenario analysis in IMF (2022), insolvent SMEs could account for up to 9% of overall SME debt. This number is consistent with the 8.8% share of MSEs (0 to 10 employees) that exited on average in the EU Member States 2019, using Eurostat data. The large discrepancy between the number of bankruptcy declarations and the number of market exits (100,000-150,000 versus 2 million) however, suggests that not all firms that exit the market are insolvent. The large number of corporations without employees or single employees that exit even suggests that a large share of the firms that exit the market do so

[239] NFC loan liabilities EU-27, 2020, non-consolidated. The sum of EUR 12,839 billion loan liabilities and 5,486 other payables. Debt securities are not added because they are hardly used by very small firms.

because the owner found employment or that the firm had fulfilled the purpose. Although it is speculative how many of the exiting firms are insolvent and how many not, it seems a conservative estimate that at least one third of the exiting firms will not enter an insolvency procedure.

- Under current conditions, one can assume that one third of the firms is rejected an insolvency proceeding, akin the share observed in Germany and Austria and that the remaining two third of the firms the judicial costs will be covered by the recovered value.

Using the Deloitte/Grimaldi estimate of cost savings and the IMF estimate of exiting firms for the upper bound and the French 50% reduction and the actual share of exiting micro firms for the lower bound, an increase in the case load by one third from the introduction of an MSE regime could lead to higher costs for the public sector between EUR 900 million and 2000 million. This number is for the EU overall and represents an overestimation since not all Member States practice the rejection of insolvency applications. A prominent example is France. The table below shows the calculation for those Member States highlighted in Deloitte/Grimaldi (2022) as using this practice. They would encounter a rising case load and when taken together face additional costs between EUR 550 milion and 970 million. Since there is no data about the number of rejected applications, except for Austria and Germany, the share of those two Member States is used for all Member States. Greece introduced an MSE regime in 2021 and once data becomes available it should be possible to refine the estimate.

Table A4.14: Assumptions and estimates for the impact of resolving asset-less MSEs in a simplified insolvency procedure

		EU	AT	BE	DE	ES	EL	IT
1	NFC debt liabilities[1)]	18324.9	397.6	862.8	3463.8	1499.1	121.0	1674.1
2	share of small loans 2[)]	0.12	0.0	0.1	0.1	0.3	0.1	0.2
3	Judicial costs [3)]	0.035	0.024	0.022	0.023	0.039	0.19	0.017
4a	Share of exiting MSEs [4)]	0.09	0.09	0.05	0.04	0.14	0.09	0.07
4b	lower bound [5)]	0.06	0.03	0.03	0.09	0.06	0.05	0.06
5	share insolvent assetless MSEs [6)]	0.33	0.33	0.33	0.33	0.33	0.33	0.33
6a	cost savings from MSE regime [7)]	0.12	0.12	0.12	0.12	0.12	0.12	0.12
6b	Higher bound [8)]	0.5	0.5	0.5	0.5	0.5	0.5	0.5
				[1]*[2]*[3]*[4] *[5]*(1-[6])				
8	lower bound[9)]	0.914	0.003	0.011	0.166	0.270	0.019	0.082
9	upper bound[9)]	2.012	0.004	0.019	0.292	0.475	0.034	0.145

[1)] Loans and other payables, Estat sectoral national accounts in EUR billion, [2)] ECB MIR, loans smaller EUR 250,000 to total loans, 12/2020 except EL (04/2021), [3)] EBA(2020), simple average 2019; [4)] Estat for firms with less than 10 employeees, 2019, except EL 2016, consistent with IMF (2022) projection, [5)] two third of the previous column as ad hoc assumption [6)] assumption based on data in DE and AT, [7)] assumption based on insolvency experts in Delotte/Grimaldi (2022), [8)] assumption based on the reduction in France from 2 years to 1 year. [9)] in EUR billion.

This calculation assumes that there is no cross-subsidisation of corporate insolvency cases. It also assumes that the judicial costs reported in EBA (2020) are sufficient to cover the cost of the insolvent proceedings for firms that were accepted for insolvency procedures, i.e. that the public sector does neither carry additional costs for the running of insolvency proceedings financed by tax payers. It also implies that the public sector will use the cost savings from the introduction of a simpler MSE insolvency regime to boost its revenues.

While the costs of an MSE regime can be substantial, it is, however, not certain whether these costs would not be outweighed by newly gained efficiencies of a more streamlined regime. These cost savings would accrue for at least there reasons. First, MSEs that already have insolvency proceedings opened (or will open them in the future) before the court under the ordinary procedure would now be able to switch to a more alleviated and quicker one, saving the costs of judicial review. Secondly, the new regime may allow for a possibility for MSEs to have a full debt discharge in an out-of-court setting, e.g. before competent administrative authorities, with faster and cheaper procedures. Thirdly and finally, the fact that currently insolvency proceedings are often not opened against MSEs does not mean they do not represent today a burden for courts and authorities. If there is no insolvency procedure, courts often have to deal with claims by creditors against that business, sometimes with multiple proceedings instead of one concentrated and simplified insolvency procedure.

4. The impact of changes in insolvency metrics on financial and economic variables

This section analyses how changes to recovery rates will feed through in financial and economic developments, applying estimates from the economic literature on the policy options at hand. The first section looks at the evidence on how the likelihood of business exits is affected since a change to insolvency regimes is expected to have an immediate effect on the number of insolvencies. The second section reviews how changes in insolvency regimes would impact the availability of credit. The empirical literature identified that better insolvency regimes improve corporates' access to finance, but this result has been found with cross-country estimates that cover a large set of countries and must not necessarily hold for the group of EU Member States.

The academic literature used legal indicators including variables that cover insolvency regimes and has consistently been able to explain them as determinant of financial and economic developments. Especially the creation of legal variables by the World Bank has initiated empirical research in this area and a number of researchers also used insolvency variables, largely in cross-country comparisons. Kliastkova and Savatier (2020) provide a survey of this literature, Closset et al (2019) also report case studies at country level. Although the World Bank Doing Business data has been discontinued, it still represents the most comprehensive data source. It covers all Member States and contains observations ranging 2004-2020 for almost all EU Member States.[240] The EBA recovery rates used in the previous section cover only one year and observations for several Member States are not representative. Hence, when doing further analysis with a panel of

[240]A panel with all EU Member States is complete for the years 2012-2020. Observations are missing for Luxembourg until 2006, Cyprus until 2008 and Malta until 2011.

EU Member States and recognition of the time dimesion, there is no alternative yet to using the World Bank data.

4.1 Business exits and economic adjustment capacity

The seminal study on legal structures as determinant of the occurrence of bankruptcies found that bankruptcies are higher the more efficient the judicial system and the more market oriented the financial system.[241] The number of bankruptcies are lower if the legal system combines a more efficient judicial system with stronger creditor rights. The more costly and lengthy the insolvency procedures, the stronger is the incentive for both debtors and creditors to keep a defaulting company afloat.[242] Empirical analysis with EU data suggests that a more efficient insolvency regime as measured by a higher recovery rate is not correlated with a higher rate of business exit or more jobs lost through business exits. If companies are in distress, however, a more efficient insolvency regime leads to a higher likelihood that they file for bankruptcy.

This first results stems from the estimates reported below that tried to determine whether World Banks' recovery rates can explain the variation of business birth rates, death rates and persons employed in exiting companies at the level of EU Member States 2004-2019. The dependent variables are Eurostat numbers of companies entering and exiting the market, and persons employed in exiting companies, relative to the number respectively employment in active companies.[243]. The estimate explains only a small share of the variation in business exits across EU Member States and time. Yet, the recovery rate is significant at 5% level with a negative sign, indicating that an increase in the recovery rate may even reduce the exit rate of companies. The magnitude of the coefficient suggests the effect is small, but at least not positive. The World Bank aggregate institutional indicator did not turn up significant when taken instead for the recovery rate in the estimate.

[241] See Claessens and Klapper (2005).
[242] See Jorda et al. (2020).
[243] The population are all firms except holding companies. This applies for the years 2007 to 2019, which is the latest observation currently covered in the Eurostat statistics. For the years 2004-2007, the data excludes holding firms, public administration and community services; activities of households and extra-territorial organizations. Control variables are GDP per capita, GDP growth, consumer price inflation, bank lending rates and dummies for the legal origin (Anglo-Saxon, French, Scandinavian).

Table A4.15: Regression results – number of business exits and outcome of insolvency procedures

Business $Exit_{ij}$ = Constant + $ß_1$ * Recovery $rate_{ij}$ + $ß_2$ * Business $exit_{ij-1}$ + $ß_3$ * Bank lending rate + μ_{ij}									
	(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Dependent variable	Number of exiting to active companyie			Share of exiting companies with more than 10 employees			Share of employment in exiting companies		
$ß_1$	-0.019	-0.019	-0.019	-0.003	-0.004	-0.005	-0.003	-0.003	-0.005
SE of $ß_1$	0.008**	0.008**	0.008**	0.002	0.002*	0.002**	0.002	0.002	0.002**
Fixed effects	none	time	time	none	time	time	none	time	time
R2	0.621	0.635	0.681	0.650	0.662	0.600	0.725	0.788	0.823
Period	2005-2019	2005-2019	2012-2019	2005-2019	2005-2019	2012-2019	2005-2019	2005-2019	2012-2019
observations	340	340	200	268	268	192	330	330	195
* significant at 10% level, ** significant at 5% level *** significant at 1% level; i, j per country i and year j.									

The result that companies in distress are more likely to file for bankruptcy the more efficient the insolvency regime stems from new analysis by the European Commission's Joint Research Centre (JRC).[244] The study uses a large panel of companies from the EU Member States 2007-2018 with almost 50 million observations. It analyses in a first stage macroeconomic and company-specific determinants of companies' bankruptcy and in a second stage whether insolvency indicators have an impact on the likelihood that a company is bankrupt. [245] Two insolvency indicators were used, the World Bank recovery rate and the World Bank time of insolvency proceedings, both yielding consistent results. For companies that are not in financial distress, the coefficient suggests a 10% pt higher recovery rate reduces the likelihood of failure by 0.004%, a 1 yeart faster recovery by 0.048%. Although the magnitude is small, the coefficients are significant at 5% level and despite the estimate controls for the sector specific bankruptcy rate and other determinants of corporat default. For companies in distress, i.e. with negative equity in the previous year, relative to healthier firms, the JRC estimates suggest that the probability of default in the short-run is larger the higher the judicial efficiency of insolvency regimes. Quantitatively, the estimated coefficients indicate that, for firms in distress, a 10% pt higher recovery rate increases the likelihood of failure by 0.5% pt relative to companies not in distress, and 1 year faster recovery time increases the relative probability of bankruptcy by 1.4% pt. Furthermore, the descriptive analysis shows that firms operating in countries with more efficient insolvency regimes are larger and more profitable, suggesting that the short run increase in bankruptcy ultimately improves resource allocation and productivity over the medium term..

The context of historically high corporate debt levels and a substantial share of EU companies with low or negative profitability led to research on how the efficiency of insolvency regimes affects economic adjustment. A more efficient insolvency regime speeds up economic recovery after recessions in Jorda et al (2020), which they link to

[244] See Fatica et al. (2022).

[245] Firms are considered bankrupt if their activity status is given as "dissolved", "in liquidation", "inactive" or "bankruptcy" or "insolvency proceedings. They are considered as in distress when showing a negative equity.

fewer zombie companies holding back productivity growth in countries with more efficient insolvency procedures.[246] Similarly, Becker and Ivashina (2021) find evidence that the number bankruptcies is higher in years with negative GDP growth when the insolvency regime ranks higher whereas such cleansing of the economy is absent in countries with weaker insolvency scores. Empirical analysis by OECD staff find a crucial role of zombie companies in weakening the adjustment process. Capital blocked in zombie companies is higher the weaker the insolvency regime, which slows down capital reallocation and ultimately the diffusion of technical progress and productivity growth.[247] Their scenario analysis finds that market exit of zombie firms would boost total factor productivity by 0.7% and 1% in Italy and Spain and up to 0.5% in other countries. The important role of insolvency regimes on the adjustment capacity of the economy is also supported by the empirical findings that insolvency regimes encourage entrepreneurship, the rate of new company entry and different proxies of economic adjustment.[248]

4.2 Credit volumes

Banks are the most common type of lenders to companies and often enjoy a privileged treatment in insolvency as senior creditors. Nevertheless, the share of other financial investors and inter-company loans in total credit provision to NFCs has been increasing over the last years.[249] The recovery value of the insolvent company's assets in an insolvency case is hence critical not only for banks, but also for an increasing number of other (alternative) providers of equity and debt financing. Furthermore, value recovery could also be relevant for other companies such as suppliers, including many SMEs. They expect to receive payments from other companies and count on providing services to them. They often suffer from their trade partner becoming insolvent, what is known the *insolvency domino effect*). SME are disproportionately vulnerable to this effect.

Since a more efficient insolvency increases the value a creditor receives in case of an insolvency, reduces the time it takes until the creditor receives this value, and/or reduces the legal costs of the proceedings, the strengthening of insolvency efficiency should foster credit provision. This factor should not be undermined by the higher likelihood that distressed companies enter into bankruptcy found in the JRC study quoted above if the shorter and more efficient insolvency process leads to a higher recovery rate. The seminal evidence that higher recovery rates would foster credit provision to the economy goes back to Djankov et al. (2008) in a panel of 84 countries. Their estimate showed a positive relationship between recovery rates and the provision of private credit,

[246] See Andrew and Petroulakis (2019) or Djankov and Zhang (2021), see also Ben Hassinem et al. (2019) for an analysis of zombie firms and insolvency procedures in France, and Gouveia and Osterhod (2018) and Nieto Carillo e al. (2022) for an analysis with Portuguese firms.

[247] Adalet McGowan, Andrews and Millot (2017a and 2017b). See also Andrews and Petroulakis (2019) and Gouveia and Osterhold (2018) for research pointing to the result that insolvency frameworks are crucal for the exit of zombie firms and productivity growth in the economy. Acharyia et al (2009) find empirical evidence that leveraged firms innovate less.

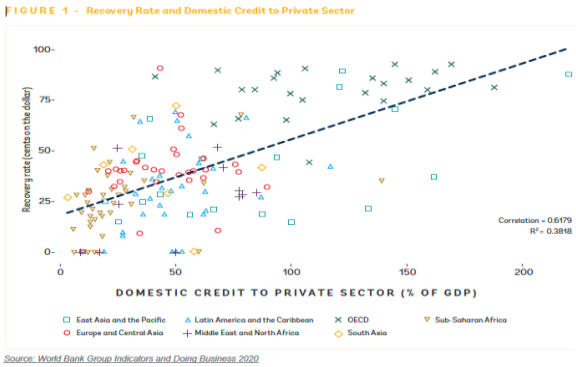
[248] See Carcera et al. (2015) for the effect on entrepreneurship, Lee et al. (2011) on firm entry and Box A1 in McGowan and Andrews (2018) for an analysis of economic adjustment.

[249] The share of bank loans to non-financial corporations in the euro area declined from above 50% of corporate loan liabilities in 2003-2012 to 43% in 2020. The share of intra-firms loans measured as the difference between consolidated and non-consolidated loans in the sectoral accounts increased from below 20% in 2003-2012 to 25%.

controlling for the influence of GDP, GDP growth, inflation, legal origin and a variable that measures the quality of the legal system.[250] The estimate suggests a 1 point increase in the recovery rate could translate into a 0.5 to 0.6 higher private credit to GDP ratio. Consistent with the results of Djankov et al, World Bank researchers recently produced the left-hand chart below, which shows a high correlation between recovery rates and credit provision to the private sector.[251]

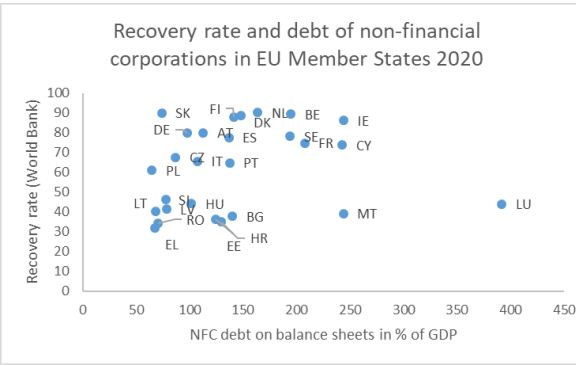
The chart on the right hand-side reproduces the World Bank chart, but with data for the EU Member States and using the debt of non-financial corporations (NFCs) instead of private credit. The focus on NFCs is more relevant for the case of this impact assessment than that of private credit because the focus of this initiative is on corporate insolvency. Moreover, the EU data allows a broader perspective than bank credit. [252] The picture is less conclusive than by the World Bank researchers. It reveals that the signs of positive correlation are clouded by the outlying observations of Malta and Luxembourg. A re-estimation of the approach by Djankov et al. (2008) with annual corporate debt flows for the EU Member States 2004-2020 also shows no clear pattern that could be used for numerical scenarios.

Figure A4.23: Recovery rate and domestic credit to private sector



Source: Uttamachandani et al. (2021).

Figure A4.24: Recovery rate and debt of NFCs in EU Member States 2020



Source: FISMA with World Bank and Eurostat data.

Causality tests undertaken in Deakin et al (2017) yielded that legal variables are impacting on the credit volume and not vice versa. Their estimates show that the direction of the impact on private credit volumes depends on whether legal reforms reduce the likelihood of default or improve creditors' right in case of a default. The former weaken shareholders position vis-a-vis the creditors and lead to higher private credit. The latter undermine the willingness of managers to provide collateral and lead to lower private credit. The researchers ran three different types of dynamic models, finding, however, that the insolvency variable is not significant in the superior type of model. Hence, they caution that the results are not definite.

[250] Days of contract enforcement.
[251] See Uttamachandani et al. (2021).
[252] Debt is calculated as loans, debt securities (bonds) and trade credit as liabilities on NFC balance sheet. Loan liabilities include loans from other counterpart than loans, for example inter-firm loans. Data taken from Eurostat's sectoral financial accounts.

Various factors suggest that there may not be a simple relationship between the efficiency of insolvency regimes and credit volumes. Already in 2008, an economic study suggest that weak credit protection induces creditors to look for compensating measures, in particular to request higher collateral.[253] The observation that newer data does not confirm the initial findings by Djankov et al (2008) of a positive relationship between the efficiency of insolvency and credit volumes might also be linked to the concerns that corporate indebtedness has reached non-optimal levels.[254] The high ratio of non-performing bank loans in the past years suggests that actual credit levels might be higher than optimal in some Member States. While more efficient insolvency regimes should support a higher sustainable level of corporate debt, it is not possible to determine the optimal level in the various Member States.

4.3 Capital costs

While the evidence that more efficient insolvency regimes increase credit supply is not conclusive, evidence that a higher recovery rates reduce corporations' costs of capital seems more robust. It is economically intuitive that a higher recovery rate reduces the risk of an investment and therewith the risk premium imbedded in the capital costs. Two investigations provide empirical support and their estimates provide indications for the magnitude of the effect.

First, AFME (2016) found a significant relationship between the recovery rate and the corporate bond spread. When taken at face value, a 1% increase in the recovery rate would reduce the bond spread by 3.7 basis points. Even when country-specific fixed effects are controlled for, the estimates suggest the effect would still be positively significant, but only half that strong.[255]

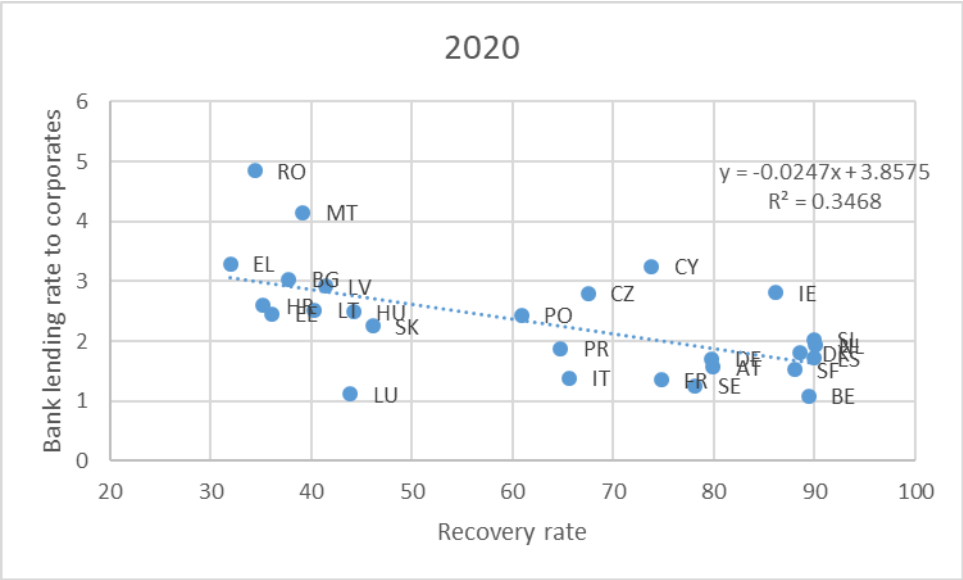
Second, IMF researchers identified that insolvency procedures are a main reason why debt funding costs of companies vary widely in background notes for the IMF (2019a, b) exploration of CMU. Differences in recovery rates explain a quarter of the observed differences in the interest expenses in a panel of companies from 22 EU Member States.[256] In an estimate that controls for capital market developments and bank lending rates, the insolvency indicator has a larger explanatory power for the remaining differences in corporate funding rates than other obstacles analysed. Differences in the recover rate explain 6% of the dispersion in funding rates for unlisted firms and 2% for listed firms. The scenario analysis of a convergence of recovery rates to the best performers yielded that funding costs would decline proportionally. A 1 percentage point increase in the variation of recovery rates translates into about 1 basis point reduction in the variation of debt interest costs.

An inverse relationship between recovery rate and bank lending rates is also visible in the chart below across the EU Member States in 2020. More detailed statistical estimates yielded a significant relationship between the recovery rate and the bank lending rate to

[253] See Davydenko and Franks (2008).
[254] See Jorda et al. (2020).
[255] Further estimates in AFME (2016) with the World Banks' aggregate insolvency score show a 1 percentage point increase in score is associated with a 27 basis points lower bond spread.
[256] The IMF researchers used interest expenses relative to debt as shown in corporate balance sheets' in a sample of almost 16000 EU firms.

corporates (1 to 5 years maturity) with a coefficient similar to the IMF estimations: A 1 percent increase in the recovery rate would reduce the bank lending rate by 1 to 1.5 basis points if a number of macroeconomic variables is controlled for. The effect on the bank lending rate is more pronounced for the recovery time than for the recovery rate.[257]

Figure A4.25: Bank lending rate and outcome of insolvency proceedings across EU Member States, 2020



Source: FISMA with ECB and World Bank data.

The estimates in the table below show a marginal immediate impact of the recovery rate and recovery time on the bank lending rate, using World Bank indicators for the EU Member States 2012-2020. The impact increases to 1 to 1.5 basis points of the recovery value when the long-term effect is considered.

Table A4.16 Regression results: interest rates and outcome of insolvency proceedings

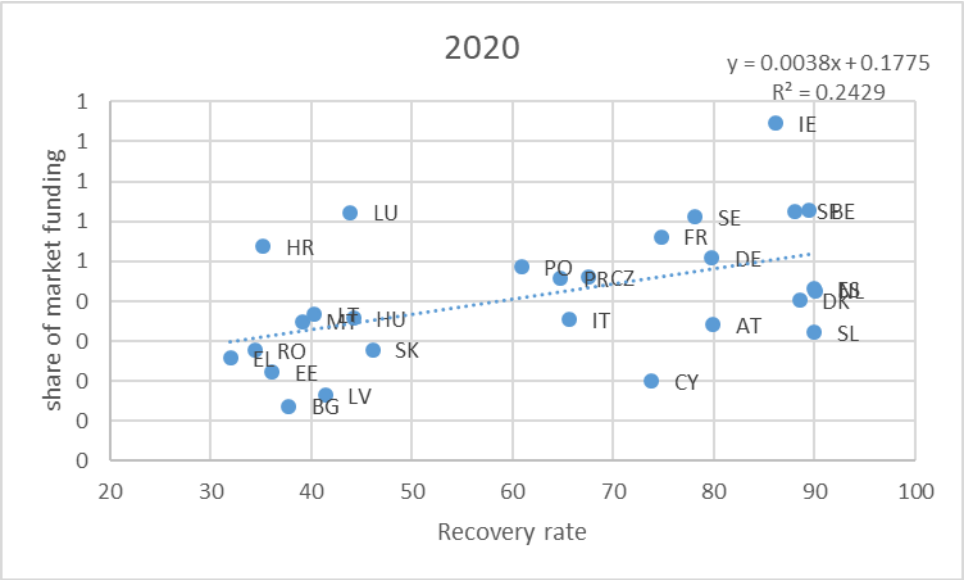
Bank lending rate $_{ij}$ = Constant + ß * Insolvency $_{ij}$ +γ_1 * government bond yield $_{ij}$ + γ_2 * bank lending rate $_{ij-1}$ + $\mu_{ij,}$				
	Recovery rate	Recovery rate	Recovery time	Recovery time
C	0.467	0.506	0.181	0.218
SE of C	0.135***	0.141***	0.070**	0.071***
ß	-0.002	-0.003	0.059	0.065
SE of ß	0.001*	0.0015*	0.031*	0.031**
γ_1		0.042		0.045
SE of γ_1		0.014***		0.014***
γ_2	0.820	0.781	0.820	0.779
SE of γ_2	0.017**	0.022***	0.017	0.022***
R2	0.92	0.92	0.92	0.93
observations	243	235	243	235

The estimates cover the period 2012-2020, other macroeconomic control variables (GDP growth, inflation, output gap) did not turn out significant and have been dropped. The lagged endogenous variable was added to address autocorrelation of residuals.

[257] The coefficient turns insignificant when both country and year-fixed effects are controlled for.

The difference in the magnitude between the AFME and IMF estimates on the impact of changes to recovery rates on corporate funding costs could be due to different reactions on corporate bond and bank lending markets. Becker and Josephson (2016) find that higher recovery rates are associated with a higher share of bond relative to bank funding. The share of bonds in companies debt funding increases by 5%-pts when the recovery rate increases by 1 standard deviation in their sample, which translates into a rise of the bond share by 0.25 %-pts for a 1 percentage point increase in the recovery rate. In a new paper, Becker and Ivashina (20121) show that better insolvency fosters the development of private debt markets.

Figure A4.26: Market funding and recovery rates across EU Member States, 2020



Source: FISMA with World Bank doing business and Eurostat data.

In view of the important role of bank credit for the financing of the European economy, the impact of insolvency regimes on bank lending appears to be an important transmission channel for the adjustment effect. In addition to the impact of insolvency on credit supply, insolvency regimes have an effect on banks' exposure to non-performing loans. Experience from EU countries in the past decade revealed that countries with weaker insolvency indicators witnessed a higher increase in non-performing loans during the sovereign debt crisis (Cucinelli et al 2018) and a more sluggish reduction after the crisis. The reason for the former is likely that banks have an interest to evergreen non-performing loans when the outcome of the insolvency process is uncertain and lengthy.[258] The latter effect was found by studies done by IMF, ECB and Commission staff.[259] Since high NPLs burden banks' balance sheet, it is intuitive that they reduce bank's capacity to lend.[260]

[258] Andrews and Petroulakis (2019) argue that the insolvency framework affects corporate restructuring also when banks are healthy because they have fewer incentives to start the process of liquidation or restructuring if insolvency procedures are cumbersome.
[259] See Consolo et al (2018), Carcera et al (2015), and Aiyar et al. (2015).
[260] In addition to their capacity to move NPLs off-balance sheets through securitisation.

4.4 Cross-border investment and risk sharing

The effects of insolvency regimes on cross border investment should be comparable to those of other institutional determinants such as investor protection, accounting standards or corporate governance for which the empirical literature established a significant link to the strength of cross-border investment.[261] Legal uncertainty acts as the main transmission channel to discourage foreign investment.

The more dissimilar the insolvency system abroad is from that in the home country, the less can domestic experiences and those made in other jurisdictions be used to assess the expected return on a cross-border investment if the debtor becomes insolvent. The consistent finding in empirical studies is that geographical distance and clusters of legal traditions[262] are important determinants of cross-border investments. This confirms the notion that familiarity matters, suggesting that the more similar the rules, the lower the threshold to engage and undertake the necessary due diligence.[263] Greater differences in substantive insolvency laws make it more costly to assess the risks of cross-border investments compared to those realised in a home Member State. High information barriers with respect to claim procedures increase the costs of legal advice.[264]

The magnitude of information and learning costs that cross-border creditors face can however be approximated through the substantial home bias in investment, i.e. the under-proportional investment in cross-border equity and debt. Home bias is evidenced in a large body of empirical research, which attributes an important role of informational frictions and uncertainty avoidance in explaining it.[265]

[261] See for example Giofre (20014), Poshakwalea and Thapa (2011), Ferreira and Miguel (2011). The legitimacy of using the results of these studies is supported by the finding in Jack (2018) that the World Banks' legal rights index is correlated with recovery rates.

[262] This is covered by a dummy variable if the home or destination country follows an Anglo-Saxon, Nordic, Latin or Germanic tradition or a dummy variable measuring a common legal origin.

[263] While familiarity appears as a factor separate from information costs in Roque Cortez et al. (2014), empirical studies tend to cover them with similar variables.

[264] On top of other costs and risks, such as language support, translating terms, general standardisation of tools, access to information. For more, please see the interviews with insolvency experts conducted by in the study conducted by Deloitte/Grimaldi (2022) on behalf of the Commission (Annex 4, Section 3).

[265] See for example, Portes and Rey (2005), Aggarwal et al. (2012). Measures of home bias of debt and equity holdings are part of the CMU indicators.

Figure A4.27: Intra EU home bias in equity

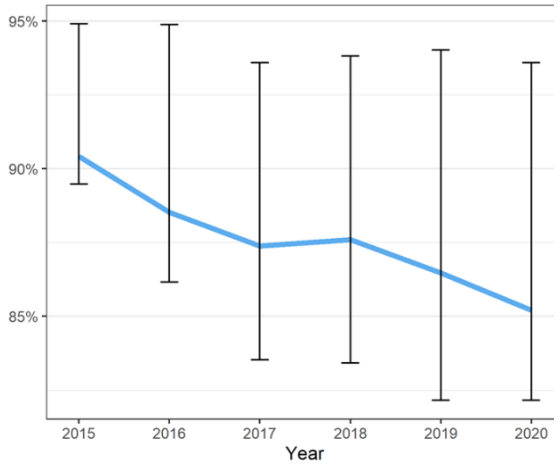
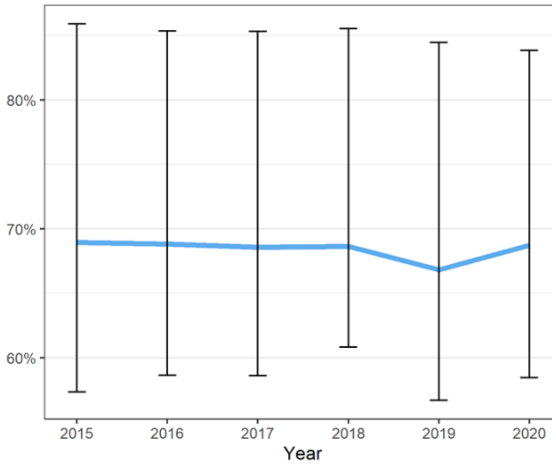


Figure A4.28: Intra EU home bias in debt securities



A declining home bias denotes improved market integration. Despite its decline 2015 to 2020, the home bias in equity remains substantial and much higher than for debt securities. The bars show the bottom and top 25% of the EU-27 Member States. JRC calculations. For an explanation, see European Commission, Monitoring progress towards a Capital Markets Union: a toolkit of indicators, SWD(2021) 544.

Source: FISMA with JRC data.

Different insolvency regimes are not only an obstacle for intra EU capital flows. Non-EU investors are equally facing a fragmented insolvency regime when they intend to invest in the EU, which creates incentives for them to concentrate on larger national markets where they can realise scale effects. The fragmentation of insolvency systems disadvantages the catch up process of smaller local capital markets. Apart from limiting the pool of capital available in the economy, underrepresentation of cross-border creditors reduces the competitive pressure on domestic market actors, with adverse consequence for the efficiency of capital allocation and funding costs.

Two recent empirical studies find evidence that insolvency regimes have a significant effect on the magnitude of cross-border investment.[266] According to the results in IMF (2019), the better the insolvency regime in destination countries, the higher are cross-border asset holdings in debt and total portfolio investment. The effect is sizeable, illustrated by the finding that cross-border portfolio assets would increase by 25% if the Italian insolvency score were to increase to the German one, i.e. by about one standard deviation. The figure blow shows that an increase of recovery rates by 25% could lead to an increase of intra-EU cross-border portfolio asset holdings by 24%.

More efficient insolvency regimes in destination countries are equally a significant determinant of cross-border asset holdings in Kliatskova and Savatier (2020). Their analysis suggests that the causality runs from insolvency to cross-border investment. Different from the IMF study are the effects stronger for equity than for debt holdings and differ across the institutional sectors holding the assets. A one standard deviation improvement in the insolvency indicator would yield 38% and 31% higher cross-border

[266] A third study is Jack (2018), who report insolvency to matter also for foreign direct investments, though without providing an empirical estimate.

assets holdings of banks and households, respectively.[267] That both studies use different data sources for measuring insolvency as well as cross border investment adds trust that the effect is material.[268]

While these two studies provide empirical evidence that insolency rules are an obstacle to capital market integration and that convergence towards more efficient insolvency proceedings would foster cross-border investments, an assessment of the importance of insolvency necessitates a comparison with other investment barriers. The main challenge for such comparisons is the need to find suitable numerical indicators for other investment barriers. It is moreover questionable how comparable an improvement in for example 1 standard deviation in the recovery rate is to a 1 standard deviation improvement in the time of law enforcement or in the tax rate or any other variable that covers obstacles to cross-border investment. The studies below endeavoured such exercise, concluding consistently that insolvency regimes are one of the most material obstacles to cross border investment.

The analysis in IMF (2019a) shows that improvements in regulatory quality have an even larger impact on cross-border capital holdings than higher recovery rates.[269] According to the scenario results, the combination of changes to insolvency rules, regulatory quality and taxation would almost double the amount of cross-border asset holdings in the euro area (180% over the baseline in Figure A4.29).

[267] The coefficient did not turn out significant for non-financial corporations and institutional investors' debt holdings. It was significant for all four sectors foreign equity holdings.

[268] IMF (2019) uses the World Bank insolvency recovery rates and the IMF Coordinated International Investment Portfolio Survey, Kliatskova and Savatier (2020) the OECD insolvency data and the ECB Security Holdings Statistics.

[269] The indicator of regulatory quality used is from the Worldwide Governance Indicators database (http://info.worldbank.org/governance/wgi/#home). This database synthesises the views of various other bodies about the quality of regulation, rule of law and other governance factors, without however a specific focus on financial regulation.

Figure A4.29: Average bilateral portfolio asset holdings after lowering obstacles in destination countries by 1 standard deviation (USD millions).

Notes: IMF staff estimates. For the insolvency indicator, 1 standard deviation equals 23.5 percentage points of the recovery rate.
Source: IMF (2019a).

Similar to Kliatskova and Savatier (2020) and consistent with IMF (2019a), Bremus and Kliatskova (2020) identify bilateral portfolio debt holdings are smaller if differences in insolvency recovery rates are larger. The estimated coefficient is significant for banks and other financial corporations as holders of portfolio debt securities, but not for non-financial actors.[270] The coefficient is also not signficiant for equity holdings. Control variables that are typically used in a gravity model such as size, distance, common legal origna etc turned out significant. Additional indicators of obstacles to cross-border investment are also significant, suggesting that they matter too. These are cross-country differences in the time to enforce a contract, coverage of credit registries and time to pay taxes. Differences in the strength of investor protection did not turn out significant. The magnitude of the effects of differences in the recovery rate and differences in contract enforcement are broadly equal, suggesting that insolvency and legal enforcement are broadly equally important obstacles to cross-border investment.

A further exercise that attempts to inform about the the relative strength of various obstacle of cross-border investment is covered in IMF (2019a). As complement to the analysis of cross-border asset holdings as a measure of capital market integration, the second analysis focuses on the impact of institutional determinants of macroeconomic risk sharing. Macroeconomic risk sharing is a consequence of capital market integration and other factors. It describes to what extent a decline in income in a country feeds through into lower private consumption. If there is no risk sharing, GDP and private consumption will grow in tandem. A number of intervening factors may however

[270] See Table 6 in Bremus and Kliatskova (2020).

smoothen the impact of a shock to GDP on consumption.[271] The standard economic parameter to do so is the exchange rate, which is however not available in a currency union such as the euro area. The literature on risk sharing demonstrated that the proportion of risks that are shared across Member States is much smaller in the euro area than across the states of the US.[272] It also shows that the difference between the euro area and the US is due to a higher contributions of cross-border capital income and – to a smaller extent –of cross-border fiscal transfers and credit markets in the US than in the euro area.

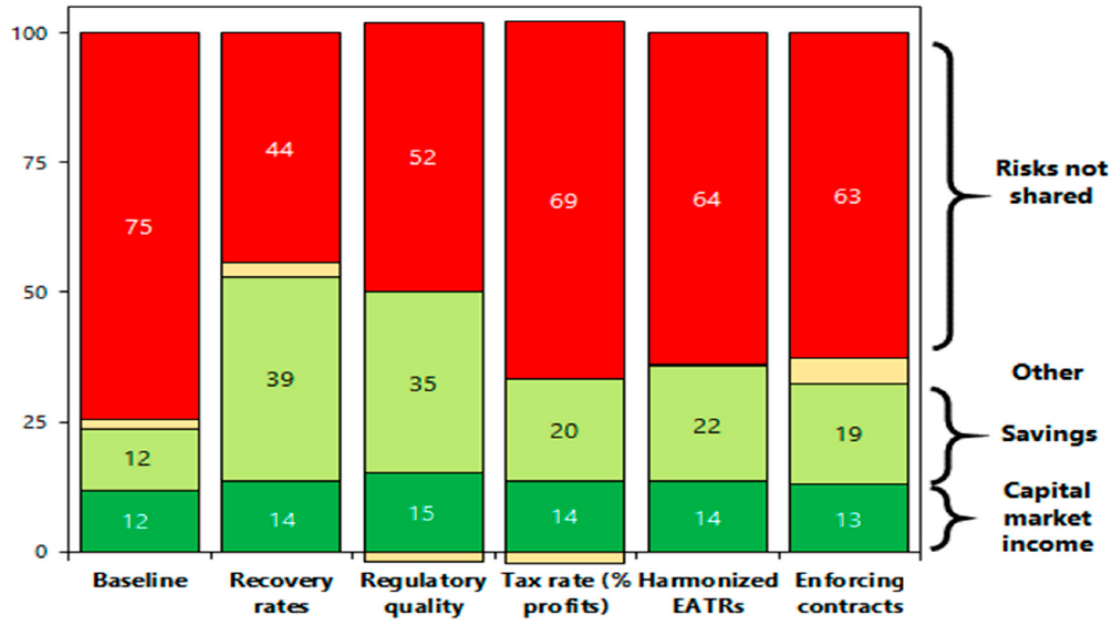
The analysis in IMF (2019a) identified a baseline for the euro area in which 75% of a negative shock to a country's GDP is not shared, i.e. a shock leads to a strong decline in consumption. Only 12% of the shock is smoothed through a higher savings (credit channel, domestic investment, credit from abroad and revenues from sales of foreign assets) and capital income from abroad (capital market channel, income from profits and earnings abroad). A comparable improvement in different institutional indicators leads to different contributions of the risk sharing channels and reductions in the share of the risk that is not shared.[273] An improvement in the recovery rate as insolvency indicator reduces the proportion of unshared risk more than other institutional reforms. It has in particular a strong effect on the credit channel, which contributes to risk smoothing through investment and lending abroad. These both factors have an intuitive relationship to the efficiency of insolvency rules

ECB staff performed similar estimates to substantiate the findings in the 2018 ECB's Financial integration report.[274] The results show a low degree of risk sharing in the euro area and small contributions of the credit and capital channel in line with the IMF estimates. Further analysis identified determinants for the strength of both channels: foreign bank penetration, financial literacy and trust for the credit channel; more cross-border investment by investment funds, private pensions and life insurance schemes for the capital channel. The empirical analysis identified a further determinant that is common to both channels: "More efficient insolvency frameworks appear to be associated with higher risk sharing via both the capital and the credit channels which persist at the European level."[275] ECB (2018) concludes "This empirical research finding shows that it is important to address the major shortcomings and divergence between insolvency frameworks which persist at the European level. This would require taking measures beyond the draft Directive on Insolvency, Restructuring and Second Chance

[271] The difference between GDP and gross national income represents the investment or capital income channel, that between gross national income and gross domestic income the fiscal channel, that between gross domestic national income and consumption the savings or credit channel.
[272] See for example, European Commission (2018), ECB (2018).
[273] The scenario assumes a decline in the z-score of different institutional indicators. The z score describes the observation of a country relative to the mean of all countries, with the scale defined through the standard deviation. The effect of a standard deviation in the z indicator of the insolvency indicator (recovery rate) can then be compared to a one standard-deviation change in z score of other institutional indicators.
[274] See ECB (2018) and Hartmann (2018).
[275] ECB (2018), p. 17.

proposed by the European Commission in the context of the capital markets union agenda".[276]

Figure A.4. 30: Relative strength of barriers in influencing risk sharing

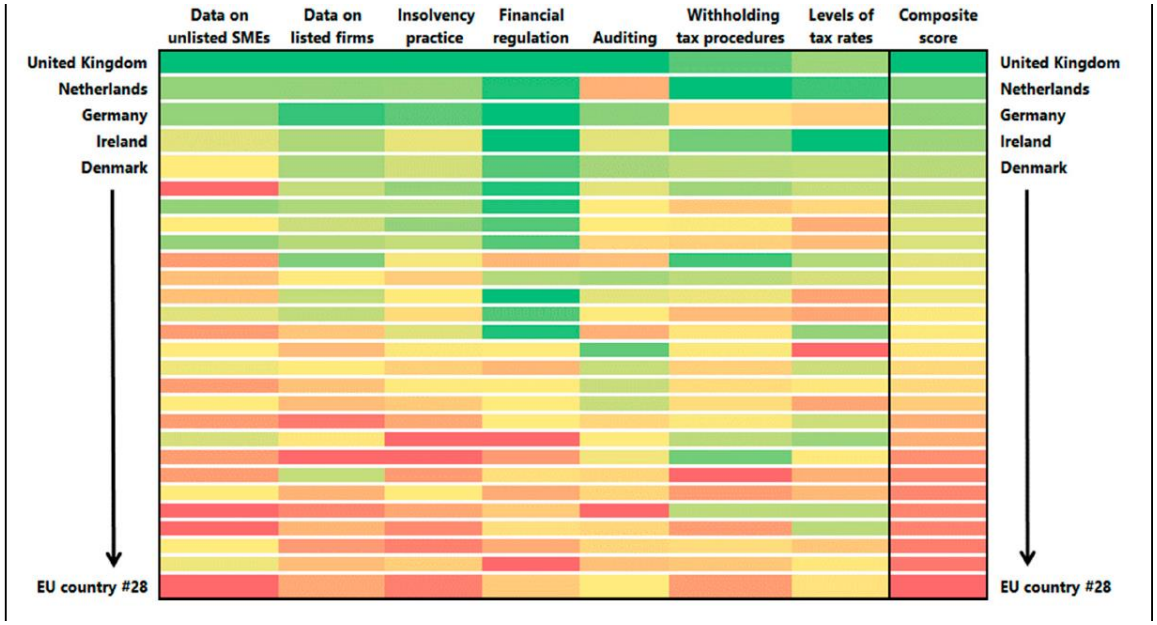


Note: IMF staff estimates. The figure shows the impact of a 1 standard deviation reduction of five barriers to capital market integration on three channels of risk sharing in the euro area. The red field indicates the share of risk that would remain unshared across Member States. Recovery rates are the indicators used to cover insolvency regimes.
Source:IMF (2019a).

IMF (2019a) complemented the empirical research by the results of a survey sent to financial market participants and national European market regulators to get views about capital market developments and deterrents to cross-border investment. Respondents were invited to score types of obstacles across Member States. The results shown in the figure below reveal that insolvency frameworks, next to data and regulatory quality was considered one of the most pressing challenge for the realisation of the Capital Market Union.

[276] ECB (2018), p. 17. See also Draghi (2018): "ECB analysis finds that where insolvency and judicial frameworks are more efficient, risk-sharing through both capital and credit markets is higher."

Figure A4.31: Results of the CMU survey conducted by the IMF



Source: IMF 2019a

Table A4.17: Economic literature with empirical estimates using insolvency indicators.

Source	Used insolvency variable	Financial or macro variable	Sample	Numerical result
Djankov et al. 2008	Recovery rate (efficiency)	Debt to GDP ratio, controls for other doing business variables, inflation, GDP and GDP/c growth, and legal origin	84 countries, average 1999-2003	A 10-point increase in efficiency is associated with a 5–6-point higher ratio of debt to GDP
Deakin et al 2017	CBC credit protection and insolvency index	Credit and bank credit	4 countries 1970-2005	Direction depends on whether legal system strengthens creditors' rights vis-à-vis shareholders or managers"
Closset et al. 2021	Dummy for restructuring reform	Cost of debt finance	15 EU Member States 2009-2014	50 bps higher costs of debt funding. Leads to cut in investment and employees pay by about 2%
AFME et al. (2016)	World Bank recovery rate and strength of insolvency framework (0-16)	Corporate bond spread	Bonds from 12 countries, 2004-2015	a 10% increase in the expected recovery rate can reduce corporate bond spreads by 37 bps (half in estimate with country dummies), a 1pt rise in insolvency score reduces the bond spread by 27 bps
IMF 2019	World Bank recovery rates	Dispersion in interest expenses in % of outstanding debt	Companys in 22 EU Member States 2015	Differences in recovery rate explain 24% of the variation in debt funding costs. An increase in the recovery rate to the UK level would reduce funding costs by 5 bps in DE, 11 bps in FR, 17 in ES, 25 in IT, 53 in EL
Becker and Josephson (2016)	Recovery rate and time from WB	Ratio of bond to bank loans in corporate funding, World bank bond market index	Companys from 44 countries 2000-2011	Coefficient of 20-25 %pt. a one-standard-deviation increase in bankruptcy recovery (22.6) corresponds to increased bond issuance by 5.6% of assets
Consolo et al. 2018	synthetic index (simple average of getting credits;	Annual change in NFC debt	40 countries 2003-2016	Countries with better insolvency frameworks deleverage faster and are able to adjust their NPL more rapidly

	recovery of debt in insolvency; (3) cost of enforcing contracts and (4) time of enforcing contracts from World Bank.			than countries with weaker regimes A 1% increase in the recovery rate reduces the change in corporate debt by 0.0028 (= 0.28 %pts)
IMF 2019	Recovery rate 2004-2017 Z value of insolv_v13	Cross border portfolio assets, i.e. ln of portfolio debt and ln of portfolio equity and total (sum of both).		1 standard deviation improvement in destination (IT to DE, or 23 ppts) yields 1.25 times increase in asset flow. Coefficient 0.0116 for ln(portfolio debt) and 00902 for ln(total)
Smrncka et al (2015)	Recovery rate	GDP per capita		Assumes reverse correlation; The recovery rate is 54+ 0.6 GDP/c implying a 1% higher recovery rate corresponds to 1.7% higher GDP/c, largely driven by countries with lower GDP
McGowan, Andrews, Millot (2017)	OECD indicator	reduce the share of capital sunk in zombie companies, and facilitate technological diffusion.		0.5% higher total factor productivity growth from the reduction of congestion with zombie firms to the lowest level per industry
Becker and Ivashina (2021)	WB aggregate insolvency index	# of private debt deals	EU Member States, UK and USA 2004-2020	a 1-point difference in insolvency restructuring score leads to 7.4 to 9.9 private deals difference
Lee et al. (2011)	WB recovery time and judicial costs, dummies for institutional characteristics	Entry of new companies	29 countries 1990-2008	A reduction in recovery time by 1 standard deviation is associated with a 10% increase in new company entry, that of 1 1 standard deviation in recovery cost with 11.3%.
Carcera et al (2015)	EC 2015 survey	Self-employment Change in non-performing loans Corporate deleveraging	EU Member States 2003-2010 and 2007-2012	A 1 %pt higher insolvency score is associated with a 0.75%pt higher self-employment rate The negative impact of corporate deleveraging on GDP growth is significantly lower in countries with superior insolvency scores
Acharya et al 2009	WB institutional indices	Patents	85 countries	Stronger creditor rights reduce innovative activity in companys
El Ghoul et al (2021)	WB institutional indices	Share of zombie firms	79 countries 20015-2016	The better the insolvency score the lower the share of zombie firms.

ANNEX 5: DETAILED DESCRIPTION OF INSOLVENCY BUILDING BLOCKS

1. Introduction

Insolvency law is considered to be a cross-cutting area of civil law that always has to strike a delicate balance between the legitimate interests of creditors and debtors, as well as between those of different types of creditors. An efficient insolvency law should help to speedily and efficiently liquidate non-viable firms and restructure (within insolvency proceedings) those that can be led back to viability and thus enable them to continue operating.

Insolvency rules should also preserve the value that can be received by creditors, shareholders, employees, tax authorities and other parties concerned, whilst ensuring an adequate balance of interests of different stakeholders. A good insolvency framework is a crucial pre-condition of credit, not only when the insolvency occurs, but also in relation to incentivizing investors to enter into a credit/debt contract. At the same time, a good insolvency framework leads to a more efficient allocation of capital within and across Member States and facilitates cross-border investments and flows of market-based finance.

This primary economic efficiency objective is complemented by specific "redistributive" goals which result from cultural and social value patterns of a given society. The insolvency legislation therefore sets out conditions for initiating insolvency procedures, outlines creditors' and debtors' rights and obligations, describes the role of courts, and the steps and the timeframe to be followed once the procedure starts.

In a cross-border context, each of the States involved has an interest in regulating insolvency of an entrepreneur whose activities or assets are located at its territory. This brings an additional source of problems of competing national interests which cannot be resolved solely by determining the applicable law and jurisdiction[277]. In reality, in a non-negligible number of situations more than one law and jurisdiction will have a competence to handle the cross-border insolvency in question: in such a case of multiplicity of laws applicable to a cross-border insolvency case, the differences between those overlapping laws will stand as a barrier to an effective solution of the cross-border insolvency case.

However, the current EU law does not harmonise any of the core features of insolvency proceedings, which remain vastly different and represent a material obstacle to the single market for creation of the Capital Markets Union. Despite these differences, insolvency frameworks in EU Member States are composed of similar building blocks. These building blocks comprise different sub-components and provide for varying solutions or rules to individual issues.

[277] Such as in the cases of Croatian Agrokor and/or Italian Parmalat examples.

Table A5.1: General description of insolvency frameworks in the EU Member States

	General insolvency framework
AT	Austrian insolvency law is not confined to entrepreneurs. Capacity for insolvency is in fact defined as a part of legal capacity under private law. Indeed, any person who can hold rights and obligations has capacity for insolvency. There is only one type of standard insolvency proceedings under Austrian law. Insolvency proceedings are known as bankruptcy proceedings, if no restructuring plan is available when the proceedings are opened. Insolvency proceedings are termed reorganisation proceedings if a restructuring plan already exists when the proceedings are opened.
BE	According to Art. 2 of the Book XX 'Insolvency of undertakings' of the Belgian Code of Economic Law (BCEL), insolvency proceedings are 'a procedure for judicial reorganization by mutual agreement or by collective agreement or by transfer under judicial authority or bankruptcy.'
BG	Insolvency and over-indebtedness are objective factual conditions, which have legal definitions in the Bulgarian Commerce Act (BCA).
HR	Under the Croatian Bankruptcy Law (CBL), there are two general regimes for debtors that are insolvent: the pre-bankruptcy settlement procedure, and bankruptcy procedure (ordinary and shortened).
CY	There are two types of insolvency proceedings: Bankruptcy and Winding-up (by the court, by creditors, under the court's supervision, receivership, arrangement or settlement or restructuring and examinership).
CZ	The individual types of insolvency proceedings (bankruptcy, reorganisation, debt relief) differ from each other in terms of the entities they are intended for. Insolvency proceedings are judicial proceedings that address a debtor's insolvency or impending insolvency and how to deal with it. The basic premise is therefore the existence of a state of insolvency or impending insolvency.
DK	Bankruptcies and restructurings (reorganisations) are governed by the Danish Bankruptcy Act (DBA), which provides for the following regimes: Restructuring; Bankruptcy; Rescheduling of debt. The restructuring and bankruptcy regime is available to insolvent individuals as well as legal entities (companies), whereas the rescheduling of debt regime is only available to individuals.
EE	Estonian legislation prescribes three different insolvency proceedings: bankruptcy proceedings, reorganisation proceedings and debt restructuring proceedings. Bankruptcy proceedings are governed by the Bankruptcy Act (BA), the rules covering reorganisation are set out in the Reorganisation Act (RA) and the debt restructuring rules are set out in the Debt Restructuring and Debt Protection Act (DPA).
FI	In Finland, insolvency laws regulate: corporate restructuring; bankruptcy; distraint; and restructuring of private debts. For companies, Finnish law recognises two statutory forms of insolvency proceedings, corporate restructuring (i.e. company administration) and bankruptcy (i.e. compulsory winding-up).
FR	Any person exercising a commercial or craft activity, any farmer, any other natural person exercising a self-employed activity, including a liberal profession, and any private law entity may be the subject of safeguard, judicial reorganisation or judicial liquidation proceedings. Safeguard proceedings are opened if the debtor is experiencing insurmountable difficulties but has not yet reached the stage of cessation of payments.
DE	Insolvency proceedings are opened only on application, and not automatically by any public body. The application can be submitted by the debtor or by a creditor. The Insolvency Code does not provide for separate types of proceedings for reorganisation and winding up. In addition to the 'standard procedure', the Code opens up the possibility of an insolvency plan as a path to winding up or as a path to reorganisation.
EL	Greece has a single, unified legal framework for efficient preventive restructuring, pre-insolvency and insolvency resolution proceedings. The newly enacted Greek Law titled 'Debt Settlement and Facilitation of a Second Chance' (Law No. 4738/2020) (the Greek Insolvency Kaw - GIL) comes into effect on 1 January 2021. An early warning electronic mechanism which classifies debtors in three (3) insolvency risk levels, low-medium-high and is supervised by the Special Secretariat for Private Debt Administration, is introduced for natural and legal persons. This tool will be able to identify circumstances that could make the debtor insolvent. The procedures under GIL are: Out-of-Court debt settlement process (Articles 5–30) GIC Under the new Out-of-Court Debt Settlement mechanism (which replaces the procedure of existing Greek Law No. 4469/2017), individuals or legal entities, eligible to be declared insolvent, may apply for extrajudicial settlement of their monetary liabilities to the Greek State or financial and social

	security institutions provided they do not fall under certain exemptions (e.g. 90% of a debtor's liabilities being owed to a single institution). The process may also be initiated by creditors with an invitation to debtors to apply within 45 days. Out-of-court settlement applications will be filed digitally to the Special Secretariat for the Administration of Private Debt through an electronic platform. Insolvency resolution process (Individuals & Legal Entities) (Articles 75–196)
HU	In Hungary, the following insolvency proceedings are available as main proceedings: bankruptcy proceedings; liquidation proceeding; and reorganization proceeding. Bankruptcy proceeding is regulated by Act XLIX of 1991 on bankruptcy and liquidation proceedings (the Bankruptcy Act). Bankruptcy is a voluntary procedure which can be initiated by the Hungarian debtor (company) by applying to the court for a moratorium over its payment obligations in order to reach a composition agreement (bankruptcy agreement) with its creditors and to continue as a going concern. If a composition agreement is reached in the bankruptcy proceedings, the liabilities of the debtor may, in theory, be discharged as provided for in the bankruptcy agreement. However, in practice, this is very rarely the case. The debtor is not required to prove that it is insolvent or over-indebted to apply for bankruptcy proceeding. Reorganization proceeding is regulated by Government Decree 345/2021. (VI. 18.).The reorganization procedure is a civil nonlitigation proceeding. It is a temporary option for the companies, since application for reorganization proceedings may be filed with the court until December 31, 2022. In terms of its purpose, the reorganization procedure is similar to bankruptcy proceedings, given that the main purpose of both institutions is to reorganize a debtor company having difficulty with payment of its debts, i.e., to restore its solvency. Regarding its material scope, reorganization may only be initiated by business organizations registered in Hungary.
IE	Insolvency proceedings are governed by the Personal Insolvency Act (PIA) and comprise the following three arrangements: Debt Relief Notice (DRN): for debts of up to €35,000 for people with virtually no assets and very low income; Debt Settlement Arrangement (DSA): for the agreed settlement of unlimited unsecured debts over a period of up to five years (extendable to six years in certain circumstances); Personal Insolvency Arrangement (PIA): for the agreed settlement or restructuring of secured debt of up to €3 million (which can be increased by creditor agreement) and unlimited unsecured debt over a period of up to six years (extendable to seven years in certain circumstances). Bankruptcy is an option for debtors who, due to their circumstances, do not meet the eligibility criteria for the abovementioned three debt solutions, or have previously entered into one of the debt solutions but the arrangement with the creditors proved to be unsustainable. As soon as a debtor is made bankrupt their unsecured debts are written off in full, however, all of their assets become the property of the Official Assignee in Bankruptcy, who is the High Court appointed administrator of the bankruptcy estate.
IT	The objective prerequisite for the declaration of bankruptcy is the state of insolvency provided for in Art. 5 of the Italian Bankruptcy Law (IBL), which establishes that a person is in a state of insolvency if he is unable to regularly meet his obligations. Insolvency can be manifested by defaults or other external facts (e.g. the escape of the entrepreneur or the closure of the premises in which he exercised the activity), which demonstrate that the debtor is no longer able to meet his obligations. An entrepreneur who can only partially pay his debts is considered insolvent, as is an entrepreneur who can fulfil his obligations, but only after they have expired, or in an irregular manner (e.g. an entrepreneur who is forced to sell real estate to satisfy the company's creditors).
LV	The insolvency proceedings of a natural person may be applied to a natural person who has been the Republic of Latvia for the last six months and who has financial difficulties (signs of insolvency).
LT	Company insolvency is understood to be a state where a company is unable to meet its obligations (does not pay debts, does not perform work paid for in advance, etc.) and the overdue obligations of the company (debts, overdue work, etc.) exceed one half of the book value of its assets.
LU	The Grand Duchy of Luxembourg has eight types of insolvency proceedings: Three apply only to traders (natural and legal persons): Bankruptcy proceeding; Composition with creditors to prevent bankruptcy; Administration proceedings. In addition to these proceedings, Luxembourg law (Article 593 et seq. of the Commercial Code) provides for a procedure whereby traders can obtain the suspension of payments under certain conditions. A fourth procedure is open only to natural persons who are not traders: this is the over-indebtedness procedure.
MT	Insolvency Proceedings (Companies) is governed by Article 214(2)(a)(ii) of Chapter 386 of the Companies Act (MCA) et seq.
NL	A debtor who is in a situation where he has stopped to pay his due and demandable debts shall be

	declared bankrupt by court order, rendered either upon his own request or upon the request of one or more of his creditors. Moreover, the bankruptcy order may also be rendered for reasons of public interest or upon the request of the Public Prosecution Service.
PL	The Bankruptcy Law identifies two independent grounds for the existence of a state of the debtor's insolvency, known as the liquidity test and the balance-sheet test.
PT	Insolvency is a factual situation of insufficiency of assets of any legal subject (insufficiency which translates into the impossibility to comply with its due obligations) described by the Insolvency and Recovery Code (Código da Insolvência e da Recuperação de Empresas - CIRE), from which may derive the adoption of a recovery measure (in the case where the insolvent party is a company).
RO	Insolvency procedure is initiated by submitting an insolvency petition in the insolvency court (the Tribunal where the debtor has its headquarter). The petition may be filed either by the debtor through its representatives, or by any interested creditor meeting the legal conditions.
SK	Insolvency means that the debtor has excessive debt or is cash-flow insolvent.
SI	Insolvency is defined as a situation where the debtor has been insolvent for a lengthy period of time.
ES	The law lays down certain subjective and objective prerequisites to be met in order to open insolvency proceedings.
SE	Insolvency is defined as a situation where the debtor is not able to duly pay his debts, and this inability is not of a temporary nature

Source: Deloitte/Grimaldi (2022).

2. Material elements of insolvency

2.1 Transaction avoidance

Transaction avoidance is a standard part of all insolvency regimes. Transaction avoidance aims at protecting the insolvency estate by clawing back on different grounds assets, that were alienated in the vicinity of insolvency. Transaction avoidance rules are aimed at the rescission of, or the compensation for, transactions that are detrimental to creditors and have been performed prior to the opening of insolvency proceedings, often in an unethical/fraudulent context.

In the run-up to insolvency, transactions might happen that are done with the intention to save certain assets from being auctioned off in insolvency. Prior to the opening of the insolvency procedure, the debtor can attribute preferential treatment to some creditors. This can lead to transactions with parties close to the owner or manager of a business, e.g. a spouse or an individual creditor with whom the business owner hopes to cooperate for a fresh start after liquidation of the business. It can also lead to transactions with undervalued prices. In order to ensure that all the debtor's assets remain available to satisfy the creditors' claims, national laws provide for avoidance actions.

The general aim of the avoidance rules is to protect the collective scheme from illegitimate alienation in the vicinity of insolvency.[278] They aim to protect the insolvent estate by providing for rescinding or offsetting transactions that were made prior to the opening of insolvency proceedings with a fraudulent intent. They define the powers granted to the insolvency practitioners to trace, freeze, confiscate and repatriate assets belonging to the insolvency estate. Transaction avoidance laws are a standard part in insolvency regimes and seek to enforce the principle of equal treatment of creditors by enabling the insolvency practitioner to challenge preferential treatment given to a creditor

[278] M Bridge, 'Collectivity, Management of Estates and Pari Passu in Winding up' in J Armour and H Bennett (eds), Vulnerable Transactions in Corporate Insolvency (Hart 2003) 18.

in a specific period prior to the application for, or opening of, insolvency proceedings. Hence, the scope of the principle of equality is extended to include a period prior to the opening of insolvency proceedings.

Avoidance rules can be categorised into[279]:

(a) legal acts compromising the estate of the debtor, further distinguishing between transactions at an undervalue and transactions not an undervalue but detrimental to creditors;

(b) legal acts in which the counterparty is already a creditor, distinguishing between payments of undue debts and payments of a debt due at the time and in the manner already agreed; and

(c) legal acts with the parties closely related to the debtors, including shareholders in view of the privileged position they have and closely related party.

The landscape in Member States is very differentiated, in all aspects of the conditions allowing for the avoidance of transactions:

(i) the legal acts to be considered (types of avoidable transactions),

(ii) the legal conditions (objective - subjective),

(iii) the length and calculation of the "suspect periods", i.e. period within which such acts can be challenged ("limitation periods"), and the consequences vary from Member State to Member State.

To date, EU legislation refers the regulation of such procedures to the national law of each individual Member State. Legal doctrine provides for multiple and different recommendations for the possible harmonisation of transaction avoidance[280]. Based on research carried out, the most promising approach appears a principle-based approach and, more specifically an approach based on the principles of equal treatment of creditors, and protection of trust[281]. An option would be to introduce harmonized rules at EU level on transaction avoidance. This full harmonisation option would not allow for deviations at national legislation for example with respect to the exemptions from the scope of legal acts concerned or the time periods It would deal with a widely known feature of insolvency law, where divergences between Member States seem to be manageable.

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[279] Rolef de Weijs, Towards an objective European rule on transaction avoidance in insolvencies, cit.

[280] Ex multis. Keay, A. Harmonisation of Avoidance Rules in European Union Insolvencies: The Critical Elements in Formulating a Scheme. Northern Ireland Legal Quarterly, 69 (2). pp. 85-106. ISSN 0029-3105, (2018). M Bridge, 'Collectivity, Management of Estates and Pari Passu in Winding up' in J Armour and H Bennett (eds), Vulnerable Transactions in Corporate Insolvency (Hart 2003) 18; Rolef de Weijs, Towards an objective European rule on transaction avoidance in insolvencies, Centre for the Study of European Contract Law Working Paper Series No. 2011/06.

[281] Approach adopted in the following studies: REPORT ON TRANSACTIONS AVOIDANCE LAWS (CERIL REPORT 2017/1), 26 September 2017, Rebecca Parry in Rebecca Parry/James Ayliffe/Sharif Shivji (eds.), Transaction Avoidance in Insolvencies, Oxford University Press, 2nd edn., Oxford 2011, para. 2.20.

While honest debtors would not undertake measures to hide assets or divert the company's at the brink of insolvency, such opportunistic behaviour at the expense of creditors cannot be excluded in individual cases and has been observed in practice. Since this behaviour is considered dishonest, other stakeholders and the general public would also value if rules on transaction avoidance were efficient. Business partners of the defaulting company would also benefit in their role as creditors, though they may face reputational costs if their financial relationships to the company become subject of scrutiny by courts or insolvency practitioners.

Since the difference of rules on transaction avoidance make it costly for creditors to find out about the respective rules in other jurisdictions and to assess the prospects for claw-back, lower diversity of these rules laws foster cross-border business, insolvency proceedings, and restructuring efforts. Stakeholders signal that the enforcement of particular cross-border assets and the detailed rules applied across Member States have led to differences in the amount that can be recovered and the time it takes to claw back assets. While insolvency practitioners are experienced in their own insolvency law, they normally have no detailed knowledge about the transactions avoidance law of the law of another Member State, which is applicable under certain circumstances to the transaction. They therefore have to commission legal opinions and to pay significant solicitor's fees when preparing the decision to start litigation against the opponent.

The harmonisation of transaction avoidance rules would be considered sensitive because of the relatedness to more fundamental principles of insolvency law. Such links exist with respect to the ranking of claims, as privileged ordinary creditors, such as tax authorities, are in some Member States exempted from transaction avoidance, too. Modifications of transaction avoidance impacts legal certainty in civil transactions since counterparts risk that a transaction with a company is under a certain risk being unwound when that company is liquidated. If the transaction has taken place under very favourable conditions, the counterpart risks facing reputation effects if a court reviews whether it was engineered to the detriment of the creditors of the liquidated company.

The principles of predictability or legal certainty and optimal realisation of the debtor's assets can conflict and must be weighed against each other. There are limits to the extent the design and application of transaction rules can be based on objective criteria. While for example, an objective criterion may be designed for the consideration of payments of an undue debt, subjective criteria are needed in many instances both to protect competing interests and to properly consider acts intentionally prejudicing creditors' rights.

Important is also the interaction of avoidance actions with restructuring of the company. Restructuring efforts may be thwarted, since the parties involved must take into account that, if the restructuring fails, insolvency proceedings ensue and legal actions which were part of the restructuring plan are subject to claw back provisions[282]. In most Member States, "safe harbour" provisions for restructuring measures are available, yet again,

[282] This statement is only valid to restructurings which are concluded outside the context of the preventive restructuring framework introduced by Title II of the Directive on Restructuring and Insolvency.

these "restructuring privileges" differ widely and still leave room for significant legal uncertainty[283].

Table A5.2: Transaction avoidance rules in EU Member States

	Transaction avoidance
AT	Certain legal acts which have been undertaken before the insolvency proceedings were opened and which are detrimental to creditors are voidable (Sec 27 et seq. AIA). The prerequisite for a successful challenge is for the legal transaction to be detrimental to the insolvency creditors. This is the case if the legal act caused a loss of satisfaction for the other creditors, for instance by reducing the assets or increasing the liabilities. A further condition for a successful challenge is that, as a result of the challenge, the prospects for satisfaction of the creditors are improved. Among the types of acts that can be subject to transaction avoidance are: voidability on account of intention to disadvantage creditors (Sec 28, numbers 1-3, AIA); voidability on account of squandering of assets (Sec 28, number 4, AIA); voidability on account of disposals free of charge (Sec 29 AIA); voidability on account of preferential treatment (Sec 30 AIA); voidability on account of knowledge of insolvency (Sec 31 AIA)
BE	Insolvency occurs from the time of the declaratory judgment of bankruptcy. The judge may advance this date by six months, if serious and objective circumstances show that the payments have already ceased before the judgment. This is called the 'suspect period'. The trustee in bankruptcy will be able to call into question transactions that occurred within this time limit and that caused any damage to the mass. The penalty consists of the transactions not being enforceable against the mass in bankruptcy. If the judge considers, at the request of the curator, that certain acts are 'suspicious' and are therefore not opposable to the mass, the person who has received the goods or has acquired them at a derisory price must return them to the mass.
BG	BCA provides for a number of safeguards that protect creditors of the insolvency estate against actions taken and transactions entered into by the debtor with a view to depleting the insolvency estate and harming creditors' interests. The law introduces the concept of a 'suspect period' — an irrefutable presumption that creditors' interests have been harmed, if certain actions have been taken or certain transactions have been entered into during this period. The suspect period commences from the date of insolvency or over indebtedness, but not earlier than one year before the petition for opening insolvency proceedings was filed, and ends on the date of the ruling opening insolvency proceedings. In other cases, it can extend to three years. A number of transactions become automatically void under article 646 BCA (e.g. settlement of a debt incurred before the ruling opening insolvency proceedings, pledge or mortgage created on a right or an asset of personal property from the insolvency estate). Other transactions can be invalidated by the court (e.g. transactions for no consideration, transactions at undervalue etc.).
HR	General: Legal acts undertaken prior to the opening of the bankruptcy proceedings that disrupt the uniform settlement of bankruptcy creditors (causing harm to creditors) or that favour certain creditors over others (preferential treatment of creditors) may be contested by the liquidator on behalf of the debtor, and the creditors in bankruptcy. There are several types of transaction avoidance: Congruent settlement; Non-congruent settlement; Legal actions by which creditors are directly damaged; Intentional damage; Legal action free of charge or with an insignificant fee; A loan which replaces capital; Secret company. Congruent settlement: Legal acts adopted in the last three months prior to the filing of a motion for

[283] A mapping of the situation in the laws of the Member States can be found in the 'Study on a new approach to business failure and insolvency, Comparative legal analysis of the Member States' relevant provisions and practices', University of Leeds, 2016, pp. 178. The Study was ordered by the Commission, hereafter: Leeds Study.

	opening of the bankruptcy proceedings / after the filing of the proposal to open bankruptcy proceedings, which provides or allows a creditor security or satisfaction in a manner and at a time that is congruent with the substance of their rights, may be challenged if, at the time of the act, the debtor was insolvent, and the creditor knew of this insolvency / knew of the insolvency or of the proposal for bankruptcy. Non-congruent settlement: A legal act that provides or allow security or satisfaction to a creditor that did not have the right to make a claim, or had no right to make a claim in that manner or at that time, may be contested: if it was undertaken within the last month prior to the filing of the proposal to open bankruptcy proceedings or after the proposal had been filed, or ; if it was undertaken within the third or second month prior to the filing of the proposal to open bankruptcy proceedings and the debtor was insolvent at the time, or; if the act was undertaken within the third or second month prior to the filing of the proposal to open bankruptcy proceedings and the creditor knew at the time the act was undertaken that it would cause harm to the bankruptcy creditors. Legal actions by which creditors are directly damaged A legal act of the debtor that directly results in harm to the creditors may be contested: if it was undertaken within three months prior to the filing of the proposal to open bankruptcy proceedings, if the debtor was insolvent at the time of the act and if the other party knew of the insolvency, or; if it was undertaken after the proposal to open bankruptcy proceedings had been filed and if the other person knew, or ought to have known, at the time of the legal act, of the insolvency or of the proposal to open bankruptcy proceedings. Intentional damage: A legal act undertaken by the debtor during the last ten years prior to the filing of the proposal to open bankruptcy proceedings, or thereafter, with the intention of causing harm to creditors, may be contested if the other party knew of the debtor's intent at the time of the act. Legal action free of charge or with an insignificant fee: A legal act of the debtor without compensation or with insignificant compensation may be contested unless it was undertaken four years prior to the filing of the proposal to open bankruptcy proceedings. In the case of an occasional gift of insignificant value, the act may not be contested. A loan which replaces capital A legal act by which a member of the company makes a claim for repayment of loan used for substituting capital, or some similar claim is void: if it provides security and if the act was undertaken within the last five years prior to the filing of the proposal to open bankruptcy proceedings or thereafter; if it guarantees the settlement and if the act was undertaken in the last year prior to the filing of the proposal to open bankruptcy proceedings or thereafter. Secret company: The return of the stake of the silent partner in a company, in full or in part, or the waiving of their share of the incurred loss, in full or in part, may be subject to challenge, if the contract on which such an act is based was concluded during the last year prior to the filing of the proposal to open bankruptcy proceedings against the company or thereafter. The same applies if the silent partner is wound up in accordance with the contract.
CY	There are a number of provisions that may invalidate a charge granted by a company or any other disposition it has made, for example: A charge that has not been properly registered is void against the liquidator and any creditor of the company (Sec 90(1), CCL) ; Any act relating to property made or done by or against a company within six months before the commencement of its winding up may be deemed a fraudulent preference if any such charge or delivery or conveyance or assignment or otherwise is a fraudulent preference of one of its creditors and such act will be invalid (Sec 301, CCL); Any gift, sale, pledge, mortgage or other transfer or disposal of any movable or immovable property made by any person with the intent to hinder or delay his/her creditors from recovering from him/her. Under these circumstances, the debts will be deemed to be fraudulent, and will be invalid and the property purported to be transferred or otherwise dealt with may be seized and sold in satisfaction of any judgment debt due (Fraudulent Transfers Avoidance Law, Cap 62); Where any part of the property of a company which is being wound up consists of immovable

	property burdened with onerous covenants, of shares or stock in companies, of unprofitable contracts, or of any other property that is unsaleable, or not readily saleable, by reason of its binding the company to the performance of any onerous act or to the payment of any sum of money, the liquidator may disclaim the property (Sec 304, CCL).
CZ	Legal acts by the debtor to reduce the chances that creditors will be satisfied or to favour certain creditors over others are unenforceable. Any omission by the debtor in this respect is also treated as a legal act. There are three categories of such unenforceable acts: legal acts without adequate consideration; preferential legal acts resulting in a situation where one creditor, to the detriment of other creditors, receives greater satisfaction than they would otherwise have obtained in the bankruptcy proceedings; legal acts where the debtor intentionally curtails the satisfaction of a creditor, if this intention was known to the counterparty or, in view of all of the circumstances, must have been known to it. The unenforceability of the debtor's legal acts is established by an insolvency court ruling on an action brought by the insolvency practitioner protesting the debtor's legal acts (an action to set a transaction aside). The insolvency practitioner may bring an action to set a transaction aside within one year from the date on which the insolvency decision takes effect. If an action is not brought within that time limit, the title to have a transaction set aside lapses. The debtor's consideration from unenforceable legal acts forms part of the estate once the ruling upholding the action to set a transaction aside becomes final.
DK	On certain conditions, the debtor's pre-insolvency transactions may be avoided by the insolvent estate. Avoidance means that an otherwise valid transaction made by the debtor is reversed if the transaction in question has defeated the assets of the estate or increased the debtor's debt. If the trustee believes that that debtor's actions are contrary to the avoidance rules of the DBA, the estate in bankruptcy must no later than 12 months from the issue of the bankruptcy order institute legal proceedings against the third party or creditor that was given preference by the debtor's voidable transaction. The debtor's voidable transactions under the DBA include: gifts from the debtor; payment of debt; transactions giving preference to a creditor over the other creditors; transactions that mean that the debtor's assets avoid being included in the assets of the estate in bankruptcy; transactions that mean that the debtor's debt increases. If the trustee is successful in the claim for avoidance against a third party, the third party must give up and return the preference to the estate in bankruptcy that s/he has obtained through the debtor's voidable transaction, but not more than the loss of the estate.
EE	After bankruptcy is declared, any dispositions by the debtor with regard to objects forming part of the bankruptcy estate are null and void. A debtor who is a natural person may dispose of the bankruptcy estate with the trustee's consent. Any dispositions without the trustee's consent are null and void. The court will revoke, by way of recovery procedure, any transaction or other act by the debtor that was concluded or performed before bankruptcy was declared and that damages the creditors' interests. If a transaction subject to recovery has been concluded or any other act subject to recovery has been performed during the period from the appointment of an interim trustee to the declaration of bankruptcy, the transaction or act is deemed to have damaged the creditors' interests.
FI	The RA sets out the general grounds for revocation of inappropriate and preferential transactions, as well as specific grounds for revocation of certain types of transactions. The RA applies in all insolvency proceedings under Finnish law, as well as in foreclosure proceedings. A transaction or any other action can be revoked where it was made during the applicable suspect period before the filing of therelevant proceedings. Under the general grounds for revocation set in Section 5 of the Recovery Act, any action made within a five-year suspect period can be revoked if: The action favours a creditor to the detriment of the other creditors, removes assets from the reach of the other creditors, or increases debt to the detriment of the other creditors; The debtor company was insolvent when undertaking the action or became insolvent as a result of it; The action was improper or inappropriate, in particular from the point of view of the other creditors of the transacting party, and the counterparty of the transacting party knew, or should have known,

	of the insolvency and the improper nature of the arrangement. Transactions that did not take place during the suspect period can only be revoked if they were made with related parties. Under the RA, a related party means a party closely related to the debtor company, including immediate family members, entities that have common (financial) interests (for example, due to shareholding or partnership), or persons that have a significant influence over the debtor due to a management or a supervisory status (RA, Section 3). For related parties, the above time limit is extended to two years.
FR	In reorganisation or liquidation, any transaction entered into during the suspect period (période suspecte) can be subject to clawback provisions. The suspect period runs from the date when the company is deemed insolvent, and can be backdated by the court by up to 18 months before the insolvency judgment. The act is void in relation to all and cancelled retroactively. There are twelve cases of compulsory nullity concerning irregular acts: all acts transferring ownership of movable property or real estate free of charge; any commutative contract in which the debtor's obligations far exceed those of the other party; any payment, by whatever method, for debts which are not due on the date of payment; any payment of debts due, other than in cash, bills of exchange, bank transfers, transfer deeds or any other form of payment commonly accepted in business dealings; any deposit or any consignment of sums made following the pledge of property, in the absence of a final court judgment; any contractual mortgage, any legal mortgage, as well as a legal mortgage of spouses, and any right of lien or pledge created on the debtor's assets for debts previously contracted; any preservation measure, unless the registration or writ of attachment predates the cessation of payment; any authorisation and exercising of options by the employees of the business; any transfer of goods or rights to a fiduciary estate, unless this transfer occurred as a guarantee for a debt contracted simultaneously; any amendment to a trust agreement affecting rights or assets already transferred to a fiduciary estate to guarantee debts contracted prior to this amendment; where the debtor is an individual entrepreneur with limited liability, any assignment or change to the assignment of an asset, subject to the payment of income not assigned to the business activity, resulting in depletion of the assets covered by the proceedings in favour of another asset of this entrepreneur; the notarial declaration of exemption from attachment made by the debtor. Any payment made, or any transaction entered into during the suspect period is also subject to optional voidance, if proper evidence is brought before the court that, at the time of the payment or transaction, the contracting party knew the company's insolvency. When dealing with intra-group transactions, this knowledge is presumed for companies belonging to the same corporate group.
DE	To prevent actions detrimental to the creditors, any acquisition of assets belonging to the insolvency estate after the opening of the proceedings is in principle void, whereas the acquisition before the opening of the proceedings of assets that would have belonged to the insolvency estate after the opening of the proceedings is in principle valid, but can be contested under certain circumstances. Since the opening of the insolvency proceedings, the right of the debtor to dispose of his property is vested in the insolvency administrator. Any disposal by the debtor of an asset belonging to the insolvency estate after the insolvency proceedings have been opened is in principle absolutely invalid (the main exception being where there is an acquisition in good faith of land, although this can be contested) (Section 81(1), first sentence, GIC). Nor is there any acquisition of rights to an asset belonging to the insolvency estate if the debtor has disposed of an asset belonging to the insolvency estate before the insolvency proceedings are opened but the result occurs only after the proceedings are opened (Section 91(1) GIC) (the main exception being an acquisition of land, Section 91(2) GIC). Rights of security acquired as a result of enforcement proceedings during the last month preceding the application to open the insolvency proceedings, or after such application, likewise become legally ineffective once the insolvency proceedings are opened (Section 88(1) GIC). An acquisition from the insolvency estate before the proceedings are opened, unlike an acquisition after the proceedings are opened, is in principle valid, but can be contested under certain conditions (Sections 129 et seq. GIC). This right to contest an insolvent debtor's transactions is of decisive importance for the functioning of insolvency law, since it allows the insolvency administrator access to outflows from the debtor's assets that took place before the insolvency proceedings are opened. It

	can help greatly to increase the insolvency estate, and thus to ensure that insolvency law makes good on its claim to provide equal satisfaction for the creditors in an orderly fashion and to prevent preferential treatment of individual creditors. If the insolvency administrator successfully exercises a right to contest, the party who benefited as a result of the contested transaction must return everything that has been withdrawn from the insolvency debtor's assets by the transaction. If he cannot do so in kind, he has to pay compensation. The insolvency administrator can bring an action to enforce the right to restitution, and can rely on the right to restitution against any opposing claims brought by a creditor. If the recipient of a benefit under a contestable transaction restores the property received, any counterclaim he may have revives (Section 144 GIC).
EL	Vulnerability of transactions is determined by reference to the date of cessation of payments, which is set by the bankruptcy court in its judgment declaring bankruptcy in respect of an insolvent debtor in accordance with the Insolvency Code. 'Cessation of payments' means the evidenced general and permanent inability of a debtor to pay its debts as they fall due. The date of cessation of payments so set by the court cannot fall earlier than two years prior to the date of the issue of the judgment declaring bankruptcy. Under Article 117 of the Insolvency Code, certain acts carried out by the debtor during the suspect period (i.e., the period commencing on the date of cessation of payments and ending on the date of the declaration of bankruptcy by the court) are subject to compulsory rescission by the bankruptcy officer. These acts include: any acts of the insolvent debtor carried out without consideration being received in return and that have the effect of reducing the value of the debtor's estate and any undervalue transactions entered into by the debtor (other than disposals made out of a moral or legal duty or as necessary to sustain the debtor's children, provided that in each case such disposals were in proportion to and did not deteriorate the debtor's financial condition); any payment of debts that are not yet due and payable; any repayment of due and payable debts not made by payment in cash or in the pre-agreed manner (other than voluntary transfers of properties to credit or financial institutions in or towards repayment of due and payable debts); and any security interest created over the debtor's assets to secure a pre-existing debt whereby the debtor had not pre-agreed to grant such a security interest, or to secure a new debt replacing a pre-existing debt (but subject to the protection accorded to security interests in favour of banks pursuant to Legislative Decree 17.7./13.8.1923). In addition, under Article 118 of the Insolvency Code, certain acts carried out by the debtor during the suspect period, which are not subject to compulsory rescission, as above, may be subject to rescission by the bankruptcy officer. Acts subject to challenge in this manner include: any payment of debts that are due and payable, and any transaction entered into by the debtor for consideration. This applies in each case if the relevant party or creditor (as the case may be) was aware of the cessation of payments and that such payment or transaction is detrimental to the other creditors. For these purposes, deemed knowledge of that party or creditor applies in respect of a spouse, close relative, founder, administrator, director, or manager of the debtor or, where that party or creditor is an affiliate of the debtor within the meaning of Article 32 of Law 4308/2014, if the terms of the transaction manifestly deviate from normal market terms. Exceptionally, certain transactions may be vulnerable even if concluded earlier than the set date of cessation of payments. Under Article 119 of the Insolvency Code, acts of the debtor concluded within the five years immediately prior to the declaration of bankruptcy are subject to rescission, if the debtor intended the act to operate to the detriment of its creditors in general or to benefit certain creditors to the detriment of other creditors, and the relevant party was, at the time of the act, aware of the debtor's intention.
HU	The administrator or creditors may challenge such transactions by lodging a petition and may request the transaction to be declared invalid. Any assets thus returned to the debtor increase the assets of the insolvent estate. Under Hungarian law, acts can be challenged within a term of 90 days before an imminent insolvency. For transactions with the intent of defrauding creditors the avoidance period is of 5 years.
IE	Insolvency Proceedings: The creditors do not have any right to seek reversal of any transactions or asset transfers prior to the commencement of the insolvency proceedings. However, if the debtor can be considered to have made excessive contributions to a pension fund, the creditor may seek financial relief from the courts. This may result in the court ordering that the fund provider issues a

	full refund of the amount for distribution among the creditors party to the arrangement. Bankruptcy: Previous asset transfers and payments that bankrupts made to creditors or other individuals can be overturned under bankruptcy legislation. This includes situations where: The bankrupt has paid an amount or transferred an asset to any creditor in preference to any other creditors to whom they owe a debt. The OA can seek to have such payments, made in the three years prior to the date of adjudication, reversed. If the OA is successful, the amount in question would be paid back into the bankruptcy estate for the benefit of all creditors; The bankrupt has transferred or gifted an asset to a third party for an amount less than the fair market value. Upon successful application before the High Court by the OA, such transfers within three years prior to the date of adjudication can be voided and the shortfall would be paid into the bankruptcy estate for the benefit of all creditors; The bankrupt has transferred an asset or made a payment which can be considered to be an 'avoidance transaction', i.e. the bankrupt was intending to avoid having the asset or sum of money considered as part of their bankruptcy estate. Two time periods apply in these cases: Any such transactions made three years prior to the bankruptcy can be reversed by the OA on successful application to the High Court, and; Any such transactions made five years prior to the bankruptcy, provided that the bankrupt fails to prove they were solvent at the time of the transaction.
IT	Legal acts carried out by the insolvent before the opening of the insolvency proceedings can be revoked if they were carried out within a certain period (one year or six months) before the opening of the proceedings. The legal references relating to the effects of legal acts carried out by the bankrupt prior to the declaration of bankruptcy which are detrimental to the mass of creditors are contained in Article 64 et seq. of the bankruptcy law. Article 64 of the bankruptcy law establishes the ineffectiveness against creditors of free acts carried out by the bankrupt in the two years preceding the declaration of bankruptcy, with the exception of gifts for use and acts carried out in fulfilment of a moral duty or in the public interest, but on condition that these gifts are proportionate to the donor's assets. Article 65 of the bankruptcy law sanctions with ineffectiveness payments made by the bankrupt in the two years preceding the declaration of bankruptcy and concerning debts due on the day of the declaration of bankruptcy or later. Article 66 of the bankruptcy law extends to the trustee in bankruptcy the right to bring an ordinary revocatory action pursuant to article 2901 of the Civil Code, in order to obtain a declaration of the ineffectiveness of the acts carried out by the debtor to the detriment of the masses, where the objective and subjective conditions exist. Art. 67 of the bankruptcy law is the pivotal rule of the bankruptcy revocation regulations contained in Section III of the bankruptcy law since it represents the main instrument for protecting the 'par condicio creditorum' and compliance with the prohibition of altering the legitimate order of privileges. The objective premise of the bankruptcy revocation action is the 'eventus damni', i.e. the very fact of the damage to the 'par condicio creditorum', which can be linked, by legal and absolute presumption, to the removal of the asset from the estate following the act of disposal. The bankruptcy law distinguishes, with regard to the subjective presupposition of the revocation action, 'normal' acts from 'abnormal' acts, i.e. acts that can be carried out in the normal course of business activity from acts that, although they can be carried out in the course of business activity, have peculiarities that lead them to real anomalies in the entrepreneur's management. If the trustee intends to apply for the revocation of 'normal' acts carried out by the debtor in the suspected period, he must prove the existence of the subjective condition of the defendant's knowledge, at the time the act was concluded, of the debtor's state of insolvency (scientia decoctionis). If, on the other hand, the trustee acts to revoke an 'abnormal' act, then he does not have to provide any evidence of the scientia decoctionis, since the law presumes that the defendant who took advantage of the abnormal act was aware of the state of insolvency of the debtor who later became bankrupt. For the purposes of the bankruptcy revocation, the liquidator must take into consideration only that part of the debtor's activity (payments, contracts, deeds, and the provision of guarantees) carried out in a period that the law considers to be 'suspicious' and that corresponds to a period of time preceding the date of the judgment declaring bankruptcy (or the date of a different order, in the event of the completion of bankruptcy proceedings). As a result of Decree-Law no. 35/2005, converted into Law no. 80/2005, the backward time limits

	for the exercise of the revocation action were halved to two years for gratuitous acts, one year for abnormal acts and six months for normal acts. As regards the starting date, the suspected period is calculated backwards from the date of publication of the declaration of bankruptcy in the company register, and not from the date of filing the judgment in the registry. Pursuant to Article 44 of the Bankruptcy Act, on the other hand, all legal acts carried out by the bankrupt and payments made by him after the declaration of bankruptcy are ineffective against creditors. Payments received by the bankrupt after the declaration of bankruptcy will also be ineffective; Finally, acts of extraordinary administration carried out by the bankrupt during agreements with creditors and without the authorisation of the court are null and void.
LV	Prerequisites for avoiding a transaction are losses incurred by the debtor (such as in the case of undervalue transactions) and knowledge of losses by the counterparty. Knowledge is presumed in the case of transactions concluded with related persons. In addition, the law vests with the insolvency administrator the right to reclaim payments made by the debtor prematurely within six months prior to insolvency, if, at the same time, other payment obligations were not honoured in time.
LT	Any transaction by the debtor that infringes upon creditors' rights may be challenged by the assigned insolvency administrator or an individual creditor, on the basis of actio Pauliana within a one-year period of limitation, which starts to run on the day when the transaction became known or should have become known. For a transaction to be successfully contested on the basis of actio Pauliana, existence of all of the following conditions is necessary: the creditor must have an indubitable and valid right of claim, i.e. the debtor must have either failed to fulfil his/her obligation entirely or must have fulfilled in improperly; the transaction at issue must infringe the creditor's rights. Creditors' rights are infringed where the transaction renders the debtor insolvent or where a solvent debtor prioritises another creditor, or the transaction, while not rendering the debtor insolvent, changes (reduces) the debtor's ability to discharge the obligation to the creditor, for instance, reduces the value of the debtor's assets (such a situation may occur, for instance, when the price received for property sold is significantly below the market price); the debtor was not obliged to enter into the disputed transaction; the debtor did not act in good faith, because he/she knew that the transaction would breach the rights of the creditors; the third party that concluded the bilateral transaction with the debtor in exchange for a compensation did not act in good faith. Additionally, at the time bankruptcy or restructuring, disposal of the debtor's property is restricted by law and the debtor's transactions concluded in violation of those restrictions are invalid as of the moment they were concluded.
LU	To protect the interests of creditors, the period between the cessation of payments and the order is regarded as the 'suspect period'. Certain acts carried out during this period, where they may be detrimental to the rights of creditors, will be null and void. These involve in particular: any acts in relation to movable or immovable property that the bankrupt has sold at no cost or in return for payment where the sale price is clearly much lower than the value of the property in question; all payments made in cash or by transfer, sale, offsetting or otherwise for debts that have not yet fallen due; all payments made other than in cash or using commercial instruments for debts falling due; any mortgage or any other property rights granted by the debtor for debts contracted before the cessation of payments. Any acts carried out or payments made in fraud of creditors, i.e. where done by the debtor in full knowledge of the detriment that this will cause to the creditor (i.e. by reducing the insolvency estate, not respecting the ranking of claims, etc.) are deemed null and void, whatever the date on which they occurred.
MT	Prejudicial transactions to creditors should address transactions undertaken by the debtor with the intention to prejudice the creditors. Currently, the suspect period in Malta is six months
NL	During bankruptcy proceedings, a liquidator may invoke the actio Pauliana to invalidate antecedent transactions that are detrimental to the insolvent estate. Clawback generally requires prejudice, which will materialise if creditors receive a lower distribution on their claims as a result of a transaction.

	Prejudice would typically be the result of a reduction in the total value of the debtor's estate as a result of a transaction (transactions at an undervalue) or as a result of a disturbance of the statutory waterfall of priorities when a company is already insolvent (preferences). The liquidator should look at the entire transaction (including beneficial aspects of the transaction) and, therefore, has no right to cherry-pick by only looking at one particular provision of a document as a clause that has a negative impact on the recourse position of the joint creditors. If the disputed act was part of a set of transactions, the positive or negative effects of the combined set should also be considered. Where prejudice has been established, the right to challenge the prejudicial action depends on further circumstances. The avoidance of an act entered into without a pre-existing obligation to perform the relevant act requires that the debtor (and in the case of a transaction against consideration, also the counterparty) knew or should reasonably have known that such prejudice would materialise. Knowledge of a mere chance that prejudice may occur is insufficient to invoke the actio Pauliana. Knowledge must relate to a reasonable degree of likeliness that insolvency proceedings will be opened, and that the insolvent estate contains a deficit. In certain cases, the onus of proof regarding knowledge of prejudice is reversed by law (e.g., in the event of certain transactions executed between related parties within a period of one year prior to the bankruptcy date). A compulsory or involuntary legal act, on the other hand, can only be avoided either in the event that the transaction occurred at a time when the counterparty knew or ought to have known that a petition was submitted for the commencement of insolvency proceedings against the debtor, or in the event of a concerted action by the debtor and the creditor aimed at facilitating preferential treatment of the latter (collusion). Finally, set-off effected in the period immediately prior to the commencement of insolvency proceedings could be clawed back if the creditor effecting the set-off acted in bad faith when acquiring its claim or debt on which it relied when setting off. Bad faith is, notably, given when the creditor knew or should have known that the insolvency could reasonably be expected. A similar rule applies to the right of an account bank to exercise its pledge over monies standing to the credit of bank accounts of its clients (such a pledge is generally stipulated in the general terms and conditions used by the relevant account bank). The pledge cannot be exercised by account banks in relation to monies paid into the account at a time when the account bank is considered to be in bad faith (as defined above).
PL	In bankruptcy proceedings the legal actions performed by the bankrupt party in respect of the bankruptcy estate are void. Under threat of nullity, the consent of the creditors' committee is required for the following actions (Article 206 of the Bankruptcy Act): the continued management of the enterprise by the receiver if it is to last more than three months after the declaration of bankruptcy; waiving the sale of the enterprise as a whole; the direct sale of the assets included in the bankruptcy estate; contracting loans or credits and encumbering the bankrupt party's assets with limited proprietary rights; the admission, waiver of entering into a composition regarding disputed claims and bringing a dispute before a court of arbitration. In restructuring proceedings, in accordance with Article 129 of the Restructuring Act, under pain of nullity the following actions by the debtor or the insolvency practitioner require the consent of the creditors' committee: encumbering elements of the composition or remedial estate with a mortgage, pledge, registered pledge or maritime mortgage in order to secure a claim not subject to composition; the transfer of the ownership of an object or a right in order to secure a claim not subject to composition; encumbering elements of the composition or remedial estate with other rights; contracting credits or loans; concluding an agreement on the leasing of the debtor's enterprise or of its organised part or another similar agreement; the sale, by the debtor, of real property or other assets worth over PLN 500 000. The insolvency practitioner may institute proceedings to declare actions invalid and other proceedings in which a claim is based on the invalidity of an action.
PT	Acts detrimental to the insolvent estate performed within two years prior to the date of commencement of the insolvency proceedings may be resolved (Article 120, no. 1 of CIRE). This

	includes all those acts that diminish, frustrate, hinder, endanger, or delay the satisfaction of creditors (Article 120.2 of CIRE). The resolution presupposes bad faith of the third party. Bad faith is understood to be the knowledge that the debtor was in a situation of insolvency; of the prejudicial nature of the act and that, on that date, the debtor was in an imminent situation of insolvency; or of the beginning of the insolvency process (Article 120, nr. 5). In any case, the bad faith of the third party is presumed when the acts performed or omitted have occurred in the two years prior to the commencement of the insolvency proceedings and in which persons especially related to the insolvent, such as parents or children, participated or benefited from (Article 120, nr. 4). In some cases, the requirement of bad faith may be waived (Article 121 of the CIRE). There are, therefore, some acts which are resolvable irrespective of any requirement. For example, the following are therefore resolvable: acts performed by the debtor free of charge in the two years prior to the commencement of insolvency proceedings (including the repudiation of an inheritance or legacy); bail, sureties, sureties, endorsements and credit mandates granted by the debtor during that period, which do not concern transactions or businesses of real interest to the debtor; onerous acts performed by the insolvent in the year prior to the commencement of the insolvency proceedings, in which he manifestly assumed more obligations than the counterparty.
RO	The following acts or transactions performed by the debtor can be annulled in order to return the transferred assets or the value of other benefits provided: acts of transfer without consideration performed in the two years prior to the opening of the proceedings; sponsorships for humanitarian purposes are exempted; unequal transactions, where what is given by the debtor is clearly greater than what is received, performed in the six months prior to the opening of the proceedings; acts performed in the two years prior to the opening of the proceedings with the intention on all sides of preventing assets from being pursued by creditors, or of harming their rights in any other way; acts of transfer of ownership to a creditor for or towards the satisfaction of a prior debt, performed in the six months prior to the opening of the proceedings, if the amount which the creditor could obtain in the event of a winding-up of the debtor is below the value of the act of transfer of ownership; the establishment of a right of preference in regard to an unsecured claim in the six months prior to the opening of the proceedings; advance payment of debts which are made in the six months prior to the opening of the proceedings, if the due date was to have been a date after the opening of the proceedings; acts of transfer or assumption of obligations performed by the debtor in the two years prior to the opening of proceedings with the intention of concealing or delaying the state of insolvency or committing fraud against a creditor. The action for annulment can be brought against a constitutive act under property law or an act of transfer of ownership under property law if it is concluded by a debtor in the normal course of its day-to-day business. An application for the annulment of a constitutive act or of an act of transfer of ownership will be entered automatically in the appropriate public registers. After the insolvency proceedings have been opened, all acts, transactions and payments performed by the debtor after the opening of proceedings are automatically null and void, with the exception the ones required for the conduct of current business, ones authorised by the delegated judge, transactions endorsed by the court-appointed administrator
SK	The Bankruptcy Act legislates for acts detrimental to the creditor by making them ineffective under certain conditions. Ineffectiveness only has consequences if the debtor's acts are contested. The insolvency practitioner and the creditors have the right to contest them, but a creditor only has this right if the insolvency practitioner does not act on the creditor's request to contest a legal act within a reasonable time. The right to contest a legal act lapse if it is not exercised in respect of the debtor or in court within a year of bankruptcy being declared; the right to contest a legal act is only considered to have been exercised in respect of the debtor if the debtor acknowledges the right in writing. Under the legislation, legal acts from which entitlements are enforceable, or have already been satisfied, can also be contested.
SI	Creditors and the bankruptcy administrator have the right to contest a legal act of the debtor. Any legal acts can be contested (including omissions) that result in unequal or reduced payment of bankruptcy creditors or in placing a particular creditor in a more favourable position. Legal acts that may be contested in bankruptcy proceedings are those that were committed in the

	period from the last year before the submission of a petition to launch bankruptcy proceedings until the opening of bankruptcy proceedings. An unpaid legal act (or legal acts of disproportionately low counter value) can be contested when committed in the period starting 36 months before the submission of the request to launch bankruptcy proceedings and ending upon the opening of bankruptcy proceedings. A lawsuit for voidability must be lodged within 12 months after a decision on opening bankruptcy proceedings becomes final. It is not possible to contest legal acts performed by the debtor in bankruptcy during compulsory settlement proceedings, in accordance with legal rules applicable for conducting the debtor's business in the proceedings; legal acts performed by the debtor in bankruptcy to pay creditor claims in the proportions, within the deadlines and at the interest rates set out in a confirmed compulsory settlement; and payments for bills of exchange or cheques if the other party had to receive a payment in order for the debtor in bankruptcy not to lose the right of recovery against another person obligated under the bill of exchange or cheque. Legal acts performed by the debtor to pay creditor claims or to perform other obligations in accordance with a confirmed agreement on financial restructuring cannot be contested either.
ES	The regulation of revocatory actions in insolvency proceedings is contained in Articles 226 et seq. of the Recast Text of the Insolvency Law. These provisions have undergone successive amendments, mainly in relation to the nature of the 'protective mechanisms' of the refinancing agreements. Article 226 contains the legal system for claw-back actions, based on a general clause declaring all acts carried out by the debtor that are 'detrimental to the assets covered by the proceedings' as 'revocable', whether or not there was 'intention to mislead'. In order to safeguard the effects of revocation, a specific period of time is established: the two years prior to the date of the insolvency order. The law opts for the establishment of a specific revocation period: two years dating back from the date of the insolvency order. Actions carried out during the 'suspect period' by the debtor are revocable if they are detrimental to the assets covered by the proceedings. Pecuniary detriment must be satisfactorily proven by the party making the complaint. However, given the difficulties normally entailed in proving detrimental acts, the Insolvency Law facilitates bringing actions through the establishment of a set of presumptions. As happens in other parts of the law, the presumptions may be irrebuttable or rebuttable. The pecuniary detriment is presumed irrebuttable in two cases: when dealing with the free disposal of assets, except donations for use, and when dealing with payments and other acts settling obligations that fall due after the insolvency order, unless they are secured by collateral, in which case the presumption admits evidence to the contrary; The pecuniary detriment is presumed rebuttable in three cases: when dealing with the disposal of assets against payment to persons with a special relationship with the insolvency debtor, when dealing with the creation of charges on property in favour of pre-existing obligations or in favour of new obligations incurred to replace the former, and payments or other acts settling obligations secured by collateral and that fall due after the insolvency order. Legal standing to bring revocatory actions in insolvency proceedings falls to the administrator. However, for the purpose of protecting creditors against the inactivity of administrators, the law provides for a subsidiary or second grade legal standing for creditors that have urged the administrator in writing to bring a revocatory action, if within a period of two months since the date of the request the action is not brought by the administrator. The law contains rules aimed at ensuring that administrators effectively carry out the role of ensuring that the assets covered by the proceedings are not disposed of. For actions against refinancing agreements, legal standing is exclusive to the administrator, excluding any subsidiary standing. In order to protect the refinancing agreements, there are special rules resulting from recent legislative amendments, which define protective mechanisms that make these agreements (approved under certain conditions) resistant to revocatory actions.
SE	An act can be reversed if it improperly favoured a certain creditor over others, or if the creditors have been deprived of the debtor's property, or if the debtor's debts have increased, and if the debtor was insolvent or became insolvent as a result of the proceeding alone or as a result of the proceeding in combination with other factors, and the other party knew or should have known that the debtor was insolvent and what the circumstances were that rendered the legal act improper.

	Payment of a debt later than three months before the reference date using a method other than the customary means of payment, or in advance, or of an amount that appreciably worsened the debtor's financial status, can be reversed unless it can be regarded as ordinary in the circumstances. If the payment was made to one of the debtor's family members prior to that date but later than two years before the reference date, it can be reversed unless it is shown that the debtor was not insolvent and did not become insolvent as a result of the act in question.

Source: Deloitte/Grimaldi (2022).

2.2 Asset tracing

Closely related to transaction avoidance, asset tracing is a "follow the money" tool, that enables courts, insolvency practitioners or parties that demonstrated a legitimate interest to determine and locate the assets, examine the revenue generated by often fraudulent activity, and follow its trail. "Asset tracing" is a legal process of identifying and locating misappropriated assets or their proceeds (values) belonging to the debtor's estate. It includes both the preservation (freezing) of the assets identified and the repatriation (if the asset is to be found in another State). [284] The effectiveness of tools for asset tracing has a key importance in the maximisation of the value of the insolvency estate. Insolvency practitioners can use the European Preservation Order Procedure ("EAPO")[285] to trace and recover assets above at least in relation to detrimental payments the debtor made to third parties. However, many aspects of EAPO implementation are governed by national laws and the main use of the instrument appears limited to tracing banking accounts[286].

Consultations with stakeholders revealed problems if a cross-border element is implied, that is the asset is situated in another Member State than the one where the proceedings have been opened. In fact, recurring feedback from the stakeholder consultation was that the means available for insolvency practitioners to trace and freeze assets belonging to the estate in another Member State are insufficient or inadequate which often results in the dissipation of those assets by the time action is taken.

Although the EU Insolvency Regulation[287] ensures that the powers of the insolvency practitioners have cross-border effects, subject to certain conditions, exercising these powers encounters difficulties in practice. Stakeholders pointed out that essential information for the purpose of asset tracing are included in national registers, but these registers are either not accessible and/or are not comprehensible by the insolvency practitioners (due to language barriers). Furthermore, information is not updated occur in practice.

[284] UNCITRAL, *Civil asset tracing and recovery in insolvency proceedings. Note by the Secretariat*, 4 October 2021 (A/CN.9/WG.V/WP.175), § 29. See previously the *Report of the Colloquium on Civil Asset Tracing and Recovery* (Vienna, 6 December 2019) (A/CN/9/1008). The documents are available at www.uncitral.org.

[285] Regulation (EU) No 655/2014 of the European Parliament and of the Council of 15 May 2014 establishing a European Account Preservation Order procedure to facilitate cross-border debt recovery in civil and commercial matters.

286 Antonio Leandro, Asset Tracing and Recovery in European Cross-border Insolvency Proceedings, 21 December 2021.

[287] EU Regulation 2015/848 of 20 May 2015 on Insolvency proceedings, hereafter EIR.

From the substantive standpoint, the current framework implies that powers of insolvency practitioners may not include coercive measures if they are not provided by the applicable law, unless ordered by a court of the specific Member State or the right to rule on legal proceedings or disputes. However, both the recognition of the powers of insolvency practitioners to act in relation to the assets located in another Member State[288] and the recognition of injunction and interim courts orders[289] are well established. Preservation measures, instead, may be adopted only where an insolvency practitioner has been appointed[290] which means that prior to the commencement of the insolvency proceedings provisional measures may be only ordered by the court upon the request of the debtor, creditors or third parties or the foreign representative[291].

Lastly, in respect to the publicity of the information regarding assets, there is a need to facilitate and speeding up the process of tracing assets for the efficiency of insolvency proceedings, in compliance with fundamental rights and data protection requirements, relying on IT tools. The EU has already taken significant steps: the EIR requires Member States to establish insolvency registers interconnected via the European e-Justice portal and to publish certain mandatory information establishing the insolvency registers' interconnection ("IRI"); the Business Registers Interconnection System ("BRIS") aims at facilitating the access to information on EU companies for the public and ensure that all EU business registers can communicate to each other; the Beneficial ownership registers interconnection system ("BORIS") serves as a central search service making available all information related to the beneficial ownership operating as a decentralised system interconnecting the national beneficial ownership registers of the Member States and the European e-Justice Portal through the European Central Platform. Lastly, there is a Proposal for a Regulation on a computerized system for communication in cross-border civil and criminal proceedings[292] (e-Codex system) which includes both the into its scope.

[288] France, Cass. Com. No. 17-16.200, Dalloz 2020, 1799, note R. Damman/A.Sallou.
[289] France, Cass. Civ. No. 15-14.664, Rev. Sociétés 2017, 303 note N. Morelli. See R. Damman/M. Guermonprez, BJE February 2018.
[290] Art. 52 EIR.
[291] Note of the Secretariat of the UNCITRAL Working Group V, 4 Ocotber 2021 (A/CN.9/WG.V/W)
[292] Proposal for a REGULATION OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on a computerised system for communication in cross-border civil and criminal proceedings (e-CODEX system), and amending Regulation (EU) 2018/1726, 2.12.2020.

Table A.5.3: Insolvency practitioners in insolvency proceedings in the EU Member States, powers relating to asset tracing are underlined

AT	**Trustee in bankruptcy proceedings:** the practical conduct of the insolvency proceedings; reviews the financial position of the debtor; continues to run the business if it is not yet closed on opening the proceedings and no disadvantage from continuation arises for the creditors; examines the claims lodged; examines whether a restructuring plan is in the interests of the creditors and whether it is likely to be executable; establishes and disposes of the assets; administers and represents the insolvency estate; exercises the right of challenge for the insolvency estate; distributes the proceeds from the estate. **Administrator in restructuring proceedings** supervises the debtor and the debtor's business management; grants or refuses authorisation for legal acts which are not carried out in the normal course of business; represents the debtor in all matters in which the debtor does not have power of disposal; ascertains the financial position of the debtor; examines whether the restructuring plan is executable and whether reasons exist for withdrawal of possession; examines the claims lodged; exercises the right of challenge for the insolvency estate.
BE	**General** The concept of 'insolvency practitioner' (IP) is defined in Article I.22, 7° of the BCEL. Belgium listed persons that, under national law, are to be considered as insolvency practitioners because they perform at least one of the tasks listed in Article 2(5) of the Regulation. The list includes: the receiver; the delegated judge; the judicial representative; the debt mediator; the liquidator; the provisional administrator. The core of the matter is set out in Article XX.20 of BCEL, which regulates the profile of insolvency practitioners, the insurance of their professional liability, the obligation to appear on the lists of practitioners provided for by the law, the methods for determining and collecting fees, the procedures for increasing or replacing fees, the procedures for increasing their number or replacing them, as well as matters relating to the end of their mandate. **Receiver** The day on which the bankruptcy is declared by the Company Court, a receiver is appointed to assume all responsibilities from the board of directors and other corporate organs. The court has absolute discretion regarding the identity and the number of receivers appointed; however, the receiver has to be a licensed insolvency practitioner registered on the list of receivers held by the court. For bankruptcies of large companies, it is not unusual to appoint a committee of receivers. The receiver has full control over the company, only subject to the oversight of the court and the judge-commissioner. **Delegated judge** If the delegated judge is included among the insolvency practitioners listed in Annex B, this does not imply that he will be subject to the rules applied by Book XX to insolvency practitioners in general. His status (like that of the judge-commissioner, who is not included in Annex B) is different from that of genuine insolvency practitioners. It is also apparent that he is not primarily responsible for any of the tasks listed in Article 2, 5 of Regulation 2015/848. **Judicial representative** The judicial representative is, in the context of a judicial reorganisation by transfer under judicial

	authority, the person responsible for organising the transfer of all or part of the undertaking. In the context of a judicial reorganisation procedure by collective agreement, a judicial representative may be appointed to facilitate the conclusion of an amicable settlement.
BG	**Receivers** Under Art. 655 of BCA, natural persons must fulfil certain conditions in order to become receivers (e.g. to have passed successfully the examination for acquiring qualification). The bankruptcy court shall appoint the receiver in bankruptcy elected by the first meeting of the creditors. The receiver in bankruptcy shall exercise his powers with the care of a prudent merchant. Under Art. 658 of BCA, the receiver in bankruptcy shall have the power to represent the undertaking and to manage its affairs. This include (the right to supervise the debtor's business, to obtain and keep the books and handle the business correspondence, to make enquiries and identify the debtor's assets, to request that contracts to which the debtor is a party be terminated, cancelled or annulled, to propose a recovery plan etc.). **Liquidators** Under Art. 266 et subseq. of the BCA, liquidators must be registered in the commercial register. Liquidators shall bear the same liability for their activities related to the liquidation as the managers and the other executive bodies of the trade companies. The liquidator shall be obliged to exercise his competencies with the care of a diligent merchant. The liquidators shall be obliged to complete any pending transactions, to collect debts due, to convert the remaining company's property into cash and satisfy the creditors.
HR	**Trustee** The trustee of the pre-bankruptcy proceeding is appointed by a decision of the court. The trustee has a number of duties, such as examining the business operations, the assets and liabilities of the debtor and the credibility of registered claims. Among others, he/she may contest claims, supervise the business operations of the debtor and file complaints to the court in cases of breaches of the CBL. **Liquidator** The liquidator in bankruptcy proceedings is selected at random and appointed by the court in the decision on opening bankruptcy proceedings. The liquidator is vested with the rights and obligations of the corporate bodies of the debtor, unless otherwise specified in the CBL. S/he is obliged to put the accounting records in order, compile a preliminary cost estimate and send it to the committee of creditors for approval, ensure the realisation of the debtor's claims, to prepare distribution to creditors and execute distribution after approval, to deliver a final account to the committee of creditors, to make subsequent distributions to creditors etc.
CY	**Compulsory winding-up by the court cases** If the court considers it appropriate, it can appoint a temporary liquidator, for the period after the submission of the petition before it and before it delivers the order of the compulsory winding-up, to protect the company's assets. The powers and responsibilities of a temporary liquidator are those that the court will give him at his appointment. The liquidator (not a temporary one) in this procedure has to ensure that the company's assets are gathered, realized, and distributed to the company's creditors, and if there is a remainder to the people entitled to it. For this reason, he has the power to proceed with almost any actions necessary to do this. There are certain actions for which the liquidator needs the permission of the court or of the supervisory committee, and there are some other actions that remain vested to the court (for instance the preparation of the contributors list, order a contributor to pay etc). The powers of the liquidator in compulsory winding-up are subject to the supervision and control of the court. **Voluntary winding-up** The liquidator in a voluntary winding-up has all the powers and responsibilities that the liquidator has in compulsory winding-up. In addition, he can proceed with certain actions relating to liquidation without the court's or the supervisory committee's permission, for which a liquidator in compulsory winding-up would need such permission. Moreover, he can perform some actions that in a compulsory winding-up would be vested to the court. However, there remain some actions for which the liquidator still needs the approval of the court or the supervisory committee. **Winding-up under the court's supervision** The liquidator's powers and responsibilities remain the same as in a voluntary winding-up, unless the court imposes restrictions. **Receivership** The powers and responsibilities of the receiver depend on and are contained in the agreement that had been previously made by the debtor and the secured creditor. **Examinership**

	The examiner has all the powers that are afforded to auditors. Moreover, s/he has the right to call for meetings and participate in them and to take measures to stop, prevent or rectify an action/omission/decision made by the company, or its creditors, or its members or its stakeholders, or by any other person, that is harmful to the company as a going concern. With the court's approval he can verify claims against the company and reach agreements for their settlement. His most important task is to prepare proposals for a scheme of arrangement or settlement or restructuring, so that insolvency can be prevented and the viability of the company as a going concern secured.
CZ	**General Insolvency administrator** General Insolvency administrator's powers: Review of the registered receivables; Drafting the list of insolvency estate (assets); Right to challenge insolvency debtor's legal actions and payments in the period up to 5 years before commencement of the insolvency proceedings; Notification of foreign EU creditors (in cooperation with insolvency court); Cooperation with the creditors' committee; Informing creditors of the economic situation of the insolvency debtor; Fulfilment of other duties imposed by the court in preliminary injunction; **Insolvency administrator powers in bankruptcy** In general – all powers of the insolvency debtor's management; Administration of the assets; Enforcement of the debtor's receivables; Sale of the assets; Payments to the creditors; Right to terminate the contracts; Administration of accounting; **Insolvency administrator powers in reorganisation** Supervision of the management of the company; Supervision of fulfilment of the reorganisation plan.
DK	The trustee has to sell the assets of the bankrupt and investigate the dispositions made in the company and thereby recover as much money as possible. The trustee is first to cover his outstanding salary for his work and then the creditors will divide the rest according to the rules in the DBA. The trustee must manage the interests of the estate to the widest extent possible, in order to ensure that the outcome of bankruptcy is as favourable as possible.
EE	A trustee in bankruptcy enters into transactions relating to the bankruptcy estate and performs other acts. The rights and obligations arising as a result of the trustee's actions belong to the debtor. A trustee, in accordance with their duties, participates in court as a party to disputes relating to the bankruptcy estate in lieu of the debtor. The trustee has the following prerogatives: determines the creditors' claims, administers the bankruptcy estate, organises its formation and sale and satisfaction of the creditors' claims out of the bankruptcy estate; ascertains the causes of the debtor's insolvency and the time when the insolvency arose; arranges for the debtor's business activities to continue, where necessary; conducts the liquidation of the debtor who is a legal person, where necessary; provides information to the creditors and the debtor in the cases prescribed by law; reports on their activities and provides information concerning the bankruptcy proceedings to the court, the supervisory official and the bankruptcy committee; performs other obligations provided for by law. If the debtor's insolvency was caused by a grave error in management, the trustee is required to lodge a claim for damages against the person liable for the error immediately after sufficient grounds for lodging a claim become evident. In addition to the trustee's rights provided for by law, a trustee also has the rights of an interim trustee. The trustee must perform their obligations with the care expected of a diligent and honest trustee and take into account the interests of all the creditors and the debtor.
FI	**Trustee in bankruptcy** The trustee has a central role in the administration of an estate in bankruptcy. The duties of the estate administrator include representing the insolvency estate, seeing to the current management of the estate, drawing up the estate inventory and the debtor description, receiving the lodgement of claims, and drawing up the draft disbursement list and the final disbursement list. The trustee also sees to the management and sale of assets belonging to the estate and disbursement of the funds. When

	bankruptcy starts, the debtor loses their authority over the assets of the insolvency estate. **Insolvency practitioner** The insolvency practitioner is responsible for realising the purpose of the restructuring proceedings and for protecting the interests of the creditors. The insolvency practitioner draws up a report of the debtors' assets and liabilities and a proposal for a restructuring programme (some other parties, such as the debtor, are also entitled to draw up their own proposal for a restructuring programme). The insolvency practitioner also supervises the debtor's activities.
FR	**Judicial reorganisation** Where safeguard or judicial reorganisation proceedings are opened, the debtor is not disinvested and continues to manage his business. Under safeguard proceedings, the court may appoint an administrator to supervise or assist the debtor in his business management, according to the mandate defined by the court in the judgment. In certain cases (businesses with at least 20 employees and turnover excluding taxes of at least EUR 3 million) that appointment is compulsory. Under judicial reorganisation proceedings, the court may also appoint an administrator (administrateur judiciaire) who will assist the debtor in his management or manage the business himself, in whole or in part, in place of the debtor. That appointment is compulsory in the same cases as in safeguard proceedings. **Judicial liquidation** In the case of judicial liquidation proceedings, the debtor is divested of the administration and disposal of his assets. The liquidator (liquidateur) exercises his rights and performs actions in relation to his business assets. The liquidator therefore undertakes the administration of his assets. **General conditions** Insolvency practitioners are court-appointed representatives placed under the supervision of the public prosecutor's office and are members of regulated professions. These specialised professionals must be entered on national lists and meet strict conditions as to suitability and good character. Persons not entered on these lists, but with particular experience or qualifications in the light of the case, may also be designated. Insolvency practitioners are appointed by the court when proceedings are opened. Insolvency practitioners could incur civil and criminal liability under ordinary law. The practitioners' fees are determined by scales fixed by decree; their remuneration under these scales is charged by the court to the debtor. **Court-appointed administrator** In principle, the court opening safeguard or judicial reorganisation proceedings appoints an administrator, who may be proposed by the debtor under the safeguard proceedings or by the public prosecutor's office. It is not compulsory to appoint an administrator if the debtor has a workforce of fewer than 20 employees and if his turnover excluding taxes is less than EUR 3 million. In the case of accelerated safeguard and accelerated financial safeguard proceedings, the appointment of an administrator is always compulsory. Under safeguard proceedings, the debtor is not disinvested and continues to dispose of and manage his assets, unless the court decides otherwise. The court-appointed administrator, if one is appointed, supervises or assists the debtor in his business management, according to the mandate defined by the court. Under judicial reorganisation proceedings, the court-appointed administrator assists the debtor in his management or manages the business himself, in whole or in part, in place of the debtor. The court-appointed administrator must take, or have the debtor take, the necessary measures to preserve the rights of the business against its debtors and the necessary measures to maintain its production capacity. The court-appointed administrator is vested with specific powers, such as operating under his signature the bank accounts of a debtor who has been prohibited from issuing cheques, requiring the continuation of current contracts and implementing the necessary redundancies. **Court-appointed receiver** It is compulsory for the court to appoint a receiver (mandataire judiciaire) in any collective proceedings. His task is to represent the creditors and their collective interests. He draws up the list of declared claims, including wage claims, with his proposals for admission, rejection or referral to the competent court, and forwards the list to the bankruptcy judge. **Liquidator** The court appoints a liquidator in the judicial liquidation order. The liquidator must verify the claims and realise the debtor's assets in order to pay off creditors. He implements redundancies and may opt for the continuation of current contracts. He represents the disinvested debtor and thus exercises

	most of his rights and performs most of the actions relating to these assets during judicial liquidation proceedings. On the other hand, he may not exercise the debtor's non-pecuniary rights
DE	The insolvency administrator is the key player in the insolvency proceedings. Only natural persons, and not legal persons, can be appointed as insolvency administrator (Section 56(1), first sentence, GIC). In particular lawyers, accountants or tax advisers come into consideration for this appointment. With the opening of the insolvency proceedings, the right to manage and dispose of the debtor's property is vested in the insolvency administrator (Section 80(1) GIC). The insolvency administrator is required to clear the assets he finds on the opening of the insolvency proceedings of any items that are not the property of the debtor. He also has to transfer to the debtor's assets items which belong to the debtor's assets under liability law, but which were not yet entered among the debtor's assets at the time insolvency proceedings were opened. The debtor's assets determined in this way constitute the insolvency estate (Insolvenzmasse, Section 35 GIC) which will be realised by the insolvency administrator and f om which the creditors will be satisfied. Further duties of the insolvency administrator include: payment of wages to the employees of the insolvency debtor, deciding whether to continue or end pending legal disputes (Sections 85 et seq. GIC) and how to deal with contracts which have not been fully performed (Sections 103 et seq. GIC), drawing up a statement of assets and liabilities (Section 153(1), first sentence, GIC), contesting transactions entered into prior to the opening of insolvency proceedings that are likely to disadvantage the ordinary creditors (Sections 129 et seq. GIC). The insolvency administrator is subject to the supervision of the insolvency court (Section 58(1) GIC). If a creditors' committee is set up, it supports and monitors the insolvency administrator in the performance of his duties (Section 69, first sentence, GIC). After the opening of the insolvency proceedings, when the right to dispose of the debtor's property has been vested in the insolvency administrator, the administrator can in principle dispose freely of all the assets belonging to the insolvency estate. There are limits on transactions of particular importance, such as the sale of the enterprise or the entire stock. Transactions of particular importance such as these require the approval of the creditors' meeting or the creditors' committee. The fact that the approval requirement has been infringed, however, has no effect on outside parties, but results only in the liability of the administrator. The administrator also has to comply with a decision of the creditors' meeting to wind up the enterprise or to continue in business (Sections 157 and 159 GIC). If the insolvency administrator wrongfully violates the obligations incumbent on him under the Insolvency Code, he is liable for damages to all parties to the proceedings (Section 60(1) GIC). Section 60(1) of the Code provides: 'The insolvency administrator shall be liable to compensate the damage suffered by any party to the proceedings if he wrongfully violates the duties incumbent on him under this Code. He shall conduct himself with the care expected of a proper and diligent insolvency administrator.' The insolvency administrator is entitled to remuneration in consideration of the exercise of his office and to reimbursement of appropriate expenses (Section 63(1), first sentence, GIC). The remuneration is regulated in the Insolvency Law Remuneration Regulation (Insolvenzrechtsvergütungsverordnung – 'InsVV') and is determined according to the value of the insolvency estate at the time the insolvency proceedings come to an end. The Regulation provides for graduated standard rates, which may, however, be increased according to the scale and difficulty of the duties of the insolvency administrator.
EL	**General** The insolvency practitioners perform specific tasks related to debt adjustment and second chance under Law 4738/2020. They must be registered in the Registry of Insolvency Practitioners. The granting, renewal and revocation of the license to Insolvency Practitioners is given by the Insolvency Administration Commission which was established on 21.4.2021 and operates within the Ministry of Finance under the supervision of the Special Secretariat for Private Debt Management. **Corporate debt adjustment through the out-of-court mechanism** In cases of corporate debt adjustment through the out-of-court mechanism: They work for the benefit of companies in order to achieve the settlement of their debts to the State, relieving the public officials of the creditors of the relevant responsibility. To this end, they provide an opinion that:

	that the assessment of the restructuring agreement provides for a recovery at least equal to the recovery in the event of the debtor's bankruptcy (and therefore that the State will not be worse off than it would be in the event of the debtor's bankruptcy); that the implementation of the restructuring agreement allows the viable operation of the company or makes it solvent, that the conditions, rules and restrictions of the debt arrangement with the State are met (e.g. that the conditions for debt writeoff are fulfilled). **Corporate debt restructuring** Insolvency Practitioners are appointed by the court as special representatives with the power to exercise some or all of the powers of the administration of the company in debt restructuring proceedings. They may also be selected by banks and loan managers to give their reasoned opinion in order to obtain the consent of the State and social security institutions to multilateral restructuring agreements for amounts owed to them exceeding EUR 1,5 million, etc. **Second chance cases** They are appointed by the court as receivers, with the power to sell all or part of the debtor's assets and subsequently distribute the resulting amounts to creditors.
HU	**Bankruptcy trustee** The court appoints a bankruptcy trustee, who shall monitor the debtor's business activities with a view to protect the creditors' interests and to prepare for the composition with creditors. Accordingly, the bankruptcy trustee shall: review the debtor's financial standing, which may entail inspection of the debtor's books, assets, and liabilities, contracts, and current accounts, requesting information from the directors of the economic operator, from the supreme body, supervisory board members and the auditor, and - in the case of a recognized group of companies governed by the Companies Act from the dominant member -, shall inform the creditors regarding his findings; carry out - assisted by the debtor - the tasks relating to the registration and categorization of claims ; approve and endorse -any financial commitment of the debtor after the time of the opening of bankruptcy proceedings; advise the debtor to enforce its claims and shall oversee the way it is executed, and in the event of the debtor's failure to comply shall notify the supreme body, the supervisory board and the auditor thereof; contest, at its discretion, any contract or legal statement the debtor has made in the absence of his approval or endorsement, and shall initiate or open proceedings for the recovery of any payments effected unlawfully or arising out of or in connection with any unlawful claim, as well as proceedings for the restoration of the situation that existed previously; categorize the registered claims and inform the creditors about the registration and categorization of their claims; exercise joint power of representation and joint right of disposition over the current accounts in the case the court orders it, or if the majority of the creditors may make the extension of the deferral period conditional on the debtor granting the trustee a joint right of representation or a joint right of disposal over the current accounts; perform the tasks of initiating the extension of payment deferral. The bankruptcy trustee shall have powers to approve any new commitment made by the debtor. However, the bankruptcy trustee may grant approval for a commitment, or for a payment, if they serve the debtor's interest in terms of operations, and for the preparation of composition arrangements, and may provide guarantees for such commitments only if agreed by the creditors representing the majority of the claims held by creditors with voting rights. The executive officers of a debtor, including its supreme body, shall exercise their respective rights only if it does not violate the powers vested in the bankruptcy trustee. The court shall impose a financial penalty on the executive officer of the debtor between

100,000 and 500,000 Hungarian forints for any breach of his statutory obligation to cooperate with the bankruptcy trustee.

Liquidator

A liquidator may only be an organization of which a member (shareholder) is known and in which a member (shareholder) does not have a direct or indirect shareholding, who is resident in a state specified in the regulation on the publication of the list of noncooperating states or in which the law does not require the tax liability corresponding to corporation tax - not including a State party to the Agreement on the European Economic Area, or the prescribed tax rate is not more than 10 percent.

The liquidator shall appoint a liquidator officer to carry out the liquidation of the debtor who has no criminal record, is not subject to a prohibition on engaging in the activity of liquidator, is not subject to a conflict of interest or meets the conditions set out in the Bankruptcy Act. This also applies to the person carrying out the tasks of bankruptcy trustee.

The rights of the owner(s) of the debtor, as defined in other regulations, shall cease as of the time of the opening of liquidation proceedings. As of the time of the opening of liquidation only the liquidator shall be authorized to make any legal statements inconnection with the assets of the debtor.

In order to perform his duties, the liquidator may enter the debtor's premises and inspect any of its assets. The debtor is obliged to open its closed areas immediately upon the liquidator's call and provide information on the existence and location of its property (furniture and other movables).

The executive officer of the debtor may be subject to a fine of up to 50 % of his income received from the debtor in question in the year preceding the time of the opening of liquidation proceedings, or up to 2.000.000 Hungarian forints, if his income cannot be determined, for failure to cooperate with the liquidator.

The liquidator shall analyse the financial standing of the economic operator and the claims against it.

If the creditors have formed a creditors' committee the liquidator shall be required to obtain the consent of the committee for continuing business operations of the debtor. The same rule applies if the creditors have selected a creditors' representative.

The liquidator may lease or transfer the debtor's assets only with the approval of the creditors 'committee or the creditors' representative or two-thirds of the creditors to a person or entity who, at the time of order of liquidation or within one year, was the executive officer of the debtor, or the debtor's sole or majority owner.

The liquidator shall have powers to terminate, with immediate effect, the contracts concluded by the debtor, or to rescind from the contract if neither of the parties rendered any services. Any claim that is due to the other party owing to the above may be enforced by notifying the liquidator within forty days from the date when the rescission or termination was communicated.

From the commencement date of the liquidation - within the framework of the law, the collective agreement and the internal regulations and employment contracts - the liquidator exercises the employer's rights and fulfils the obligations. The liquidator collects the debtor's claims when they fall due, enforces its claims and sells its assets. The liquidator is obliged to take care of the protection of the debtor's property during the liquidation proceeding. The liquidator is obliged to ensure the preservation of the debtor's records and documents.

The liquidator shall act with the due diligence expected of the person holding such office. He is liable for damages caused by a breach of his obligations under the rules of civil liability. The liquidator is liable for the debtor's assets existing at the commencement of the liquidation or acquired during the liquidation.

One of the liquidators' due diligence is that if an unlawful asset withdrawal from the debtor has taken place in the period before the insolvency of the debtor has been declared, and the liquidator considers that action against such unlawful withdrawal may increase the liquidity of the debtor, it must initiate proceedings to reclaim such asset, and inform the creditors' committee.

Reorganization expert

The assistance of a reorganization expert is mandatory in the reorganization proceeding. Only the National Reorganization Non-Profit Limited Liability Company may act as a reorganization expert.

The reorganization expert shall immediately review the financial situation of the debtor after the commencement of the reorganization proceeding and shall be informed of all circumstances affecting the planned reorganization.

The reorganization expert is involved in negotiating the reorganization plan with creditors. During the reorganization, the senior executive of the company is obliged to co-operate with the reorganization expert, facilitate the performance of his duties and provide him with all the

	information and documents necessary for the performance of his duties. During the reorganization, the executive officer of the company is obliged to report to the reorganization expert on the fulfilment or challenging of debts due during the moratorium period, the necessary measures that have been taken to enforce the company's claims, as well as and if the company is in arrears of more than 20 days with its payment obligations not covered by the moratorium. The reorganization expert may get acquainted with the data and documents of the company containing business secrets and other private secrets for the purpose necessary for the performance of his duties, the exercise of his rights and the fulfilment of his obligations. The reorganization expert is entitled to make a statement to the creditor providing new or temporary financing about the investment risk of the company's situation and the reorganization plan. As part of the reorganization plan, creditors may stipulate that the reorganization expert will monitor the implementation of the reorganization plan and report to the creditors, and the company must tolerate the control and cooperate with the reorganization expert. If the reorganization plan requires the reorganization expert to monitor the implementation of the plan, the reorganization expert has an obligation to report to the decision-making body of the company and to the creditors involved in the reorganization plan. It shall immediately notify the decision-making body, the supervisory board and the auditor of the undertaking, as well as the interim or new financiers, if the undertaking is in arrears with its payment obligations for more than 30 days or if it fails to take action to enforce its claims.
IE	**General** The PI Act creates a new profession regulated by the ISI, which falls into two categories: Approved Intermediaries (AIs): a person or corporate body authorised by the ISI to support debtors who wish to make an application for a DRN; Personal Insolvency Practitioners (PIPs): a person authorised by the ISI to act as liaison between the debtor and their creditor(s) for the purposes of securing a DSA or PIA. A PIP is legally obliged to act in compliance with the PI Act and associated regulations. **Insolvency Proceedings** A PIP, when engaged by a debtor, will act as a negotiator between the debtor and their creditors. PIPs are bound by legislation to act in the best interests of both the debtor and the creditor(s), therefore they are obliged to formulate the best possible arrangement for all parties concerned in an insolvency arrangement. The role and functions of a PIP include: Engaging with a debtor who is contemplating making a proposal for an insolvency arrangement; Accepting the appointment to act as insolvency practitioner; Reviewing the Prescribed Financial Statement (PFS) prepared by the debtor and providing advices to the debtor on options and their eligibility to make a proposal for a debt settlement or personal insolvency arrangement; Satisfying themselves that the financial information provided to them by the debtor is accurate and complete; Providing an opinion, based on the criteria set out in legislation, as to which type of insolvency arrangement (DSA or PIA) best suits the debtor's situation; Providing information relating to the procedure chosen, the general effect of, and the likely costs of becoming a party to an insolvency arrangement; Applying on behalf of the debtor for a Protective Certificate (PC); Notifying all creditors of the PC, PIP appointment, enclosing a copy of the debtor's PFS; Preparing a proposal to creditors and convening a statutory meeting of creditors to consider and vote upon the proposal; Where a proposal is approved, notifying the ISI and all creditors of the outcome; Once approved by court or on a court review, operating the terms of the arrangement including the collection of funds from the debtor and payment to creditors over the duration of the arrangement; Monitoring the arrangement throughout its lifetime; Carrying out a review of the arrangement on at least an annual basis; In insolvency proceedings, the debtor's role is to participate honestly in the process, agree to the arrangement negotiated by their PIP and meet the required terms of the arrangement. **Bankruptcy** On adjudication in bankruptcy, all assets divest from the bankrupt and vest in the Official Assignee (OA) in Bankruptcy. The OA is an independent statutory officer whose role is to administer

	bankruptcy estates and manage the Bankruptcy Division of the ISI.In Ireland, a private individual can be appointed as trustee in bankruptcy to replace the High Court Official Assignee in Bankruptcy (OA). In practice, such appointments are extremely rare. The Bankruptcy Act does not specify any qualifications for such appointments. The debtor's powers in bankruptcy are limited to being able to apply to the High Court to challenge certain decisions of the OA. The debtor has an obligation to comply with requests made by the OAs office with regard to the administration of the bankruptcy estate.
IT	**Curatore** The insolvency practitioner (curatore) has the power/duty to manage the assets, sell them, and distribute the proceeds to the creditors. The curator is appointed by the judgment declaring the bankruptcy, or in case of replacement and revocation by court decree. The law requires certain positive requisites in order to be appointed. In fact, the following may be called upon to carry out these functions pursuant to Article 28 IBL: lawyers, accountants and bookkeepers; associated professional studios or companies between professionals; those who have carried out functions of administration, management and control in joint stock companies. **Liquidator** The liquidator is called upon to carry out the following tasks: to affix the seals on the bankrupt's assets and draw up the inventory; draw up the first information report on the causes of the economic breakdown; draw up, every 6 months, a report summarizing the activities carried out ; draw up the balance sheet for the bankrupt's last financial year; examine applications for admission to the liabilities; attend the hearing for the discussion of the statement of liabilities; examine applications for admission to the liabilities which are submitted late; to present a request to the court which orders the non-prosecution of the statement of liabilities due to insufficient realization of assets; prepare a liquidation plan; submit a statement of available funds every 4 months; present a management report; promote the closure of the bankruptcy; propose to the delegated judge, in order to obtain authorization, the leasing of the bankrupt's company or company branches to third parties.
LV	An administrator shall be appointed by a court on the basis of a nomination by the Insolvency Administration immediately after the initiation of an insolvency matter. The Insolvency Administration chooses and recommends one administrator candidate by the principle of accident. An administrator has many duties according to the Latvian Law. He or she shall: Ensure that the insolvency proceeding proceeds lawfully and effectively; Assume the property, documentation and seal of the debtor until termination of the insolvency proceedings or the entering into of a settlement; Administer the property of the debtor during the insolvency proceedings and ensure its maintenance until the termination of the insolvency proceedings and the payment of money intended to cover the costs of administration and debts, or the entering into of a settlement; Ascertain the causes of actual insolvency and provide his or her opinion regarding them to the creditors' meeting and the court; File to the Insolvency Administration information and documents about insolvency proceedings in accordance with the Insolvency Administration's requirements, etc.
LT	**Bankruptcy proceedings** Under corporate bankruptcy proceedings, the appointed bankruptcy administrator takes over the company's management, disposes of its estate, organises the sale of the estate and settles with creditors using the proceeds, and takes any steps necessary to wind up the company. The key functions of the corporate bankruptcy administrator are as follows: to represent the company and to defend its interests and those of all its creditors; to take over the management of the company in bankruptcy and the bankruptcy estate; to terminate company contracts that will no longer be implemented (including contracts with members of the management bodies and staff); to apply for money from the Guarantee Fund in order settle up with creditors/employees;

	where necessary, to enter into temporary work or service contracts required for the purposes of the bankruptcy procedure; to verify the creditors' claims filed and to submit the list of these for approval by the court; to oversee the business operations of the company in bankruptcy; to check the company's transactions entered into over the three-year period prior to the institution of the bankruptcy proceedings; to dispute the company's transactions in court if they are contrary to the company's operating objectives and may have contributed to the company's inability to pay its creditors; where justified, to apply to the court to have the bankruptcy declared intentional; to convene creditor meetings; to draft activity reports and to submit them to the meeting of creditors; to compile and deliver the company's annual and intermediate financial statements; to implement the decisions of the court and the creditors' meeting; to provide information on the bankruptcy procedure; to organise the sale of the bankrupt company's assets; to use the funds obtained in the course of the bankruptcy procedure to settle up with the creditors; to perform any actions necessary to wind up and unregister the company. **Restructuring proceedings** In the case of a company restructuring, the assigned restructuring administrator acts as a professional consultant and independent person in control of the restructuring procedures. The key functions of the restructuring administrator are as follows: to contribute to the drafting and consideration of the company's restructuring plan and to take measures to ensure that the restructuring plan is drafted, submitted for approval and implemented within the deadlines set by the court; to prepare a written conclusion on the feasibility of the draft restructuring plan; to oversee the activities of the management bodies of the company being restructured in as far as they relate to the implementation of the restructuring plan, to notify the members of the company's management bodies of iv) the shortcomings found in their activities and set a deadline for rectifying these, and to apply to the court for removal of the management bodies of the company; to convene meetings of the company's members, owners of the representatives of the body exercising the rights and obligations of the owner of a State or municipal enterprise and to participate in those meetings without voting rights; to supply information concerning the restructuring proceedings and to inform the court about the progress of the restructuring plan. The restructuring administrator, together with the management bodies of the company being restructured, are responsible for the implementation of the court-approved restructuring plan. In the case of bankruptcy of a natural person, the assigned bankruptcy administrator disposes of the assets of the natural person organises their sale, and uses the proceeds to settle with the creditors. The key functions of the natural person bankruptcy administrator are as follows: to dispose of the assets of the natural person and the funds in the deposit account; to keep the accounts of all the funds received by the natural person and of the use thereof; to organise the sale of the natural person's assets and settle up with the creditors; to convene creditor meetings and take part in them without voting rights; to provide information on the bankruptcy procedure for the natural person and to deliver the restoration plan implementation report; to initiate amendments to the solvency restoration plan; to represent the natural person in proceedings for recovery of assets on behalf of the natural person in bankruptcy and take action to recover debts from the debtors; to defend the rights and legitimate interests of the natural person and all creditors; to evaluate the expediency of a natural person's self-employment and/or farming activities.
LU	Trustees in a bankruptcy represent both the bankrupt person and the body of their creditors. In this dual capacity, they not only are responsible for administering the bankrupt's assets, but are also authorised to monitor, as claimants or defendants, all actions that seek to preserve the assets that must be used as security for the creditors, and also to recover or increase those assets in the common interests of the latter. The trustee may bring any actions in respect of the common security for the creditors, consisting of the bankrupt's assets seek to recover, protect or liquidate those assets.
MT	**Winding up proceedings** The insolvency practitioner in a winding up by the court shall, have the power:

	to sell the movable and immovable property, including any right, of the company by public auction or private agreement with power to transfer the whole or any part thereof; to do all acts and to execute, in the name and on behalf of the company, all deeds, receipts and other documents; to raise on the security of the assets of the company any money requisite; to appoint a mandatory to act for him in his capacity as insolvency practitioner for particular purposes. **Reorganisation proceedings** In Reorganization Proceedings, during the period that a recovery (reorganization) order is in force, the company shall continue to carry on its normal activities under the management of the special controller. The special controller needs to be an individual who the Court has ascertained to its satisfaction that he/she enjoys proven competence and experience in the management of business enterprises, is qualified and willing to accept the appointment, and has no conflict of interest in relation to his appointment. The special controller has the authority to: take into his custody or under his control all the property of the company and he shall thenceforth be responsible to manage and supervise its activities, business and property; after informing the Court, to remove any director of the company and to appoint any individual to serve as a manager; engage persons for the provision of professional or administrative services, and commit the company to the payment of their respective fees or charges; and to call any meeting of the members or creditors of the company. **Bankruptcy proceedings** In case of Bankruptcy, the special controller has the power to: take possession of all the bankrupts' property and rights of any kind belonging to the bankrupt; take all the necessary steps to preserve the rights of the bankrupt against his debtors; register in the Public Registry any hypothec affecting the property of the debtors of the bankrupt. Within one month from the delivery of the judgment of bankruptcy, s/he shall make up an inventory of the bankrupt's property
NL	The court will appoint an administrator. The debtor must inform the administrator about everything that might be relevant for its situation. Often the administrator will end debtor's business and sell its company's assets.
PL	In bankruptcy proceedings, after the declaration of bankruptcy the receiver draws up an inventory, estimates the bankruptcy estate and drafts a liquidation plan. The liquidation plan defines the proposed manner of selling the bankrupt party's assets, in particular the enterprise, the time of the sale, an estimate of expenditure and the economic rationale for the continuation of the business activity (Article 306 of the Bankruptcy Act). After drawing up the inventory and financial report or after submitting a general written report the receiver liquidates the bankruptcy estate (Article 308 of the Bankruptcy Act). After the liquidation the receiver may continue to manage the bankrupt party's enterprise if a composition with the creditors is possible or if it is possible to sell the whole of the bankrupt party's enterprise or organised parts thereof (Article 312 of the Bankruptcy Act).
PT	**General** According to Article 2 of the Statute of the Judicial Administrator (Law No. 22/2013, February 26) 'the judicial administrator is the person in charge of the supervision and guidance of the acts integrating the special revitalization process, as well as the management or liquidation of the insolvent estate under the insolvency proceeding, being competent to perform all the acts committed by this statute and by the law.' As follows from Art.2, no. 2 of CIRE, the judicial administrator may have three different designations, depending on the functions he performs in the proceedings: **Insolvency administrator** In view of the lack of confidence in the debtor's administrative capacity, which the debtor's insolvency naturally implies, it is necessary to appoint an insolvency administrator, i.e., an autonomous administrator of the debtor, who has, among other duties (Article 55 of CIRE), the powers to administer the insolvent estate. Thus, with the judgment of declaration of insolvency, the CIRE requires the appointment of an 'Insolvency Administrator' or reappointment of the 'Provisional Judicial Administrator', whose role, in collaboration and under the supervision of the judge and the creditors' committee (if any, since it is an optional body in the process), is to administer the insolvent estate, proceeding with the recovery of the company or its liquidation. **Provisional Judicial administrator** In the special revitalization process (PER) and in the special process for payment agreement (PEAP),

	having as competencies, according to Article 33 of CIRE, the maintenance and preservation of the debtor's assets, providing for the continuity of the company's operation, unless he considers that the suspension of activity is more advantageous to the interests of creditors and such measure is authorized by the judge. The provisional judicial administrator is thus only in charge of assisting the debtor in the administration of his assets. **Fiduciary** During the assignment period (5 years) regarding the discharge of the remaining liabilities, after the granting and opening of the process for the discharge of the remaining liabilities (Art.235 et seq. of CIRE), the Trustee is appointed as Fiduciary acting only as a supervisor of the process, verifying that the insolvent who requested the discharge of his liabilities complies with the plan determined by the Court and not having any executive power, as results from Art.241 of CIRE, under the heading 'Functions'.
RO	The authorities and responsibilities of the Romanian insolvency practitioners arise, in the first place, from the provisions of the Government Emergency Ordinance no. 86/2006 on the organization of their activity. Under the applicable rules, insolvency practitioners have a number of powers and responsibilities both in insolvency prevention and in bankruptcy proceedings; moreover the Insolvency Office Holders (IOHs) also play an important role in the ordinary procedures for the dissolution and the liquidation of companies according to the Companies Law no. 31/1990. The Government Emergency Ordinance no. 86/2006 specifies the functions of IOHs, as follows: the Judicial Administrator is the insolvency practitioner appointed to fulfil duties provided both by law or assigned by the court during the observation period and the reorganization procedure; the Judicial Liquidator is the insolvency practitioner appointed to control the debtor's activity within the bankruptcy procedure and to perform other duties provided by the law or assigned by the court; the Composition Administrator is the insolvency practitioner appointed to perform the tasks provided by the law or assigned by the court, within the preventive composition procedure; The 'ad hoc agent' (in Romanian language 'Mandatarul ad hoc') is the insolvency practitioner appointed to perform the tasks set out by the law or the ones assigned by the court, within the out-of-court settlement with creditors procedure.
SK	**General duties** Insolvency practitioner primarily manages the assets subject to bankruptcy proceedings, realises them and uses the proceeds to pay the debtor's creditors. When the bankruptcy order is made, the debtor's right to dispose of assets subject to bankruptcy proceedings and the right to act on the debtor's behalf in matters concerning these assets pass to the insolvency practitioner, who now acts in the name and for the account of the debtor. Insolvency practitioners' duties are to: produce a list of assets in the bankruptcy estate and disposes of them (i.e. the assets subject to the bankruptcy proceedings); terminate certain contracts; realise the assets from the estate, pays the costs of the bankruptcy proceedings, proposes the distribution schedule for the proceeds, and subsequently implements it; if the bankruptcy proceedings use a payment schedule, to draft the payment schedule and submits it to the court for approval. **Role in case of reorganisation** In case of reorganisation, the insolvency practitioner's main role is to draft the reorganisation plan in collaboration with the debtor and the creditors. S/his duties are to: examine the claims lodged and establishes or denies them; supervise the debtor.
SI	**Receiver** In accordance with the provisions of ZFPPIPP the receiver shall be a body in insolvency proceedings, executing its competencies and tasks in such proceedings, stipulated by an Act, with the aim of protecting and realising the interests of creditors. In insolvency proceedings, the receiver shall conduct the operations of the insolvent debtor according to the needs of the procedure, and represent him: in procedural and other legal actions in relation to testing claims, to rights to separate satisfaction and exclusion rights; in procedural and other acts in relation to rebutting the legal actions of the insolvent debtor; in legal transactions and other acts necessary for the realisation of the bankruptcy estate;

	in realisation of the right to dispose of the claim and other rights acquired by an insolvent debtor as legal consequences of the initiation of bankruptcy proceedings, and; in other legal transactions which the insolvent debtor may carry out pursuant to ZFPPIPP. The receiver shall perform his tasks and competencies in accordance with ZFPPIPP and regulations issued on the basis thereof, other acts which apply for an insolvent debtor, and regulations issued on the basis thereof and the rules of the profession of persons who execute operations for other persons as mandataries. In performing his tasks and competencies, the receiver shall act conscientiously and fairly, with a corresponding professional care, and so as to protect and realise the interests of creditors, which shall be the guide in executing such tasks and competencies. The receiver shall treat creditors who are in an equal position vis-a-vis the insolvent debtor, equally and shall not enable or allow that individual creditors in the procedure achieve priority payment or other benefits to the detriment of other creditors who are in an equal position vis-a-vis the insolvent debtor, or that other persons obtain the insolvent debtor's assets which belong to the bankruptcy estate without providing for an equivalent counter performance, or other benefits to the detriment of the bankruptcy estate which are not in accordance with acts, regulations and rules of the profession mentioned above. The receiver shall prepare a regular report on the conduct of the procedure every three months. The receiver shall submit a regular report to the court in compulsory settlement proceedings within eight days, and in bankruptcy proceedings within one month following the end of the period to which the report refers. Upon a request by the court or creditors' committee, the receiver shall submit a written report on a certain matter significant for the conduct of the procedure, or protection, or realisation of interests of creditors in such procedure (extraordinary report), within eight days following the receipt of the request, unless a longer time limit for submission is determined in the request. A presiding judge shall instruct the receiver on the work which are obligatory for him. **Liability of the receiver** The receiver shall be liable to creditors for any damages incurred as a result of a violation of his obligations. The receiver shall be liable to creditors for the damages referred to in the previous sentence, caused in an individual insolvency proceeding, up to five times the amount of entitled remuneration from such procedure, but not less than EUR 5,000.
ES	The functions of the insolvency administrator are limited by the type of insolvency proceeding in which he acts, so that in the case of a compulsory insolvency proceeding the administrator will replace the debtor in the exercise of his powers of administration and disposal of the estate, while in the case of a voluntary insolvency proceeding his actions will be limited to simple intervention in the functions of the company's management board, whose actions will be subject to his consent. The administrator is a necessary person that assists the judge and is entrusted with managing the insolvency proceedings. Once insolvency proceedings have been opened, the judge orders the initiation of phase two of the proceedings, which includes everything relating to the appointment, provisions governing, powers and responsibilities of the administrator. The administrator is chosen from among the natural and legal persons voluntarily registered in the Public Insolvency Register in accordance with the conditions established by law. Insolvency practitioner has a series of duties, such as: duties of a procedural nature; duties relating to the debtor or its governing bodies; duties regarding labour matters; duties relating to creditors' rights; report and evaluation duties; duties relating to the realisation or liquidation of assets; secretarial duties. Their most important duty is to submit the report provided for in Article 292, to which they must add an asset inventory proposal and the list of creditors
SE	**Bankruptcy** Once a bankruptcy decision is announced, the debtor loses control of any property pertaining to the bankruptcy estate. The debtor may not enter into any obligations that might be invoked during the bankruptcy. There are some exemptions. During the bankruptcy process the bankruptcy estate is represented by the administrator. The administrator is appointed by the district court, and must have the special knowledge and experience required for the task, and be suitable for the task in other respects. A person employed by a court may not be appointed as an administrator. A person may not

	be appointed as an administrator if they have a conflict of interest. **Business reorganisation** A business reorganisation officer must have the special knowledge and experience required for the task, must have the confidence of the creditors, and must be suitable for the task in other respects. The business reorganisation officer investigates the debtor's financial standing and, in consultation with the debtor, draws up a plan setting out how the aims of the reorganisation are to be achieved. The plan must be supplied to the court and to the creditors. The business reorganisation officer may engage expert assistance. The debtor is required to provide the business reorganisation officer with all information concerning his or her financial circumstances that is relevant to the restructuring of the business. The debtor must follow the business reorganisation officer's instructions concerning the manner in which the business is to be run. There are some legal acts that the debtor cannot perform without the business reorganisation officer's consent. These include paying debts that arose prior to the decision, undertaking new obligations, and transferring or pledging property of substantial importance for the debtor's business. If the debtor fails to fulfil these obligations, however, the legal act in question remains valid.

Source: Deloitte/Grimaldi (2022).

2.3 Duties of directors (and liabilities) of companies to file for insolvency

Directors owe a series of duties to the companies to which they are appointed. Overall, beside their general duties, directors are subject to other duties enshrined in insolvency law, such as fraudulent trading and wrongful trading.[293] Directors of companies have a duty to act in the best interests of the company, seeking to avoid insolvency and in the "likelihood of insolvency", directors should change their point of view and consider within their duties also the interests of the creditors.[294] Specifically, if there is a likelihood of insolvency, directors need to:

(a) take immediate steps to minimize the loss for creditors, workers, shareholders;

(b) have due regard to the interests of creditors and other stakeholders;

(c) take reasonable steps to avoid insolvency; and

(d) avoid deliberate or grossly negligent conduct that threatens the viability of business.

In the event of a "serious loss of the subscribed capital", directors have the duty to convene the shareholders' meeting to take the best appropriate action (Article 58 of Company Law Directive (EU) 2017/1132). For example, the German public company legislation provides a duty for the directors if "upon preparation of the annual balance sheet or an interim balance sheet it becomes apparent, or if in the exercise of proper judgment, it must be assumed that company has incurred a loss equal to one half of the

[293] Carsten Gerner Beuerle and Edmund – Philipp Schuster, „*The evolving Structure of Directors' Duty in Europe*" (2014) *European Business Organisation Law review 15, p. 224*

[294] World Bank Principle B.2. clearly states that "Laws governing directors' obligations in the period approaching insolvency should promote responsible corporate behaviour while fostering reasonable risk taking and encouraging business reorganization. The law should provide appropriate remedies for breach of directors' obligations, which may be enforced after insolvency proceedings have commenced. The World Bank, Principles for Effective Insolvency and Creditor/Debtor regimes, 2021.

share capital, the management board shall promptly call a shareholders' meeting and advise the meeting thereof".[295]

In case of non-compliance with such obligation to file for insolvency within a predetermined maximum time limit, directors could be held personally liable for the losses incurred by creditors as a result of the delay in the opening of the insolvency procedure as compared to a timely filing. The nature of the liability varies across Member States and will usually involve, at least, civil liability to creditors for loss of company assets/funds that resulted from failing to file for insolvency on time. In jurisdictions where the obligation of directors does not change with the advent of vicinity to insolvency, directors are not free to act as they wish. Many of these jurisdictions - in fact - provide that director can be held liable for a form of wrongful trading, i.e., if the director continues to operate the company without mitigating the to minimize losses to creditors[296]. In other jurisdictions, while directors of a company are not subject to specific corporate or bankruptcy law restrictions, they can be held liable for wrongful trading by creditors of the company. For example, in the Netherlands, directors could be subject to tort action by a creditor with whom they contracted on behalf of the company when the directors knew or should have known that the company would not be able to meet its obligations to the creditor or have sufficient assets to discharge the obligation to the creditor[297].

Even where commonalities exist, the concrete solutions diverge: e.g. when the company meets the conditions of being insolvent, duties of the directors vary in the Member States as to the type of action they have to take, the time limits within which they have to act or the consequences they face in case of breaching this duty (e.g. civil liability for damages of the creditors. Where jurisdictions place less emphasis on shareholders and more on a range of stakeholders, if a company is on the verge of insolvency, it has been suggested that it could be left to the courts to balance the interests of stakeholders and consider the financial position of the company[298].

The conduct of the directors in the vicinity of insolvency is key in terms of influencing the prospects of value maximization and recovery rate in the concrete proceedings. Differences in national laws add to legal uncertainty for cross border investors. Differences in the duties and liability of directors can also incentivise companies to engage in forum shopping, i.e. relocating the company's centre of main interest (COMI) shortly before the commencement of insolvency proceedings with the aim to achieve a more lenient treatment under the new applicable law.

Concretely, an alerting mechanism to induce more cognitive behaviour for directors (thereby justifying eventual sanctions against reckless/wrongful behaviour) could be

[295] Aktiengesetz article 92(1)

[296] Article 2394 and 2086 Italian civil Code.

[297] The relevant rule in the Netherlands is called the "Beklamel-rule" and named after the case that decided that directors could be liable on the basis discussed in the article: C. Garner-Beuerle, P. Paech and E. Schuster, "Study on Directors' Duties and Liability" April 2013, London, LSE, and prepared for the EC, at p351.

[298] Alessandra Zanardo "*Fiduciary Duties of Directors of Insolvent Corporations: A comparative Perspectives*" (2018) Chicago-Kent Law review 93.

introduced and/or a shift of fiduciary duty to be owed to the creditors of the debtor (instead of the shareholders) when the debtor is insolvent or insolvency is imminent. Such a rule would be challenging as conflicting existing approaches of national company/insolvency laws.

Table A5.4: Rules on directors' duties in EU Member States	
AT	If the managing directors (or certain other legal representatives) of the entity fail to file for the commencement of insolvency proceedings in time, they face exposure to claims by creditors and the insolvent entity. Under the Austrian Company Reorganisation Act, managing directors are liable vis-à-vis the company for liabilities not covered by the eventual insolvency estate if, within the last 2 years before the insolvency filing, they: have received a report from the company's auditor stating that the equity ratio (Eigenmittelquote) is less than 8% and the notional debt repayment period (fiktive Schuldentilgungsdauer) exceeds 15 years, and they have not immediately filed for reorganisation proceedings or have not properly continued them, or; have not prepared annual financial statements, or have not done so in a timely manner, or have not immediately commissioned the auditor to audit the annual financial statements.
BE	In case the company is declared bankrupt, the directors can be held liable: for a part or all the debts of the bankruptcy, if it can be demonstrated that they made a gross error that contributed to the bankruptcy; for a part or all debts of the bankruptcy, if the directors did not file for bankruptcy although it was clear that there was no reasonable prospect of continuing the activities and avoiding a bankruptcy (wrongful trading); for certain social and tax debts, if the directors during the last 5 years prior to the bankruptcy were involved in at least two other bankruptcies in which there were unpaid social and tax debts.
BG	There are no specific provisions with regards to liability and the responsibilities of directors during insolvency proceedings. General rules apply. According to Art. 237 of the BCA, 'the members of the boards shall be obliged to perform their functions with the care of a diligent merchant in the interest of the company and all stockholders.' Under Art. 240 of the BCA, the members of the boards shall be jointly and severally liable for any damages caused through a fault of theirs.
HR	The CBL rendered more stringent rules on directors' liability for insolvency related duties, i.e. for a timely filing of the petition to open bankruptcy proceedings. Directors are required to initiate bankruptcy proceedings within 21 days from the moment the bankruptcy reason occurred. In certain cases the liquidator, supervisory board members and each shareholder are also required, to file request for opening bankruptcy proceeding. Failure to initiate bankruptcy proceedings when required is considered a criminal offence under the Croatian law. Furthermore, failure to initiate bankruptcy proceedings within the set time frame by the responsible person means he/she shall be personally liable for damages caused to creditors for failure to fulfil his/her duty. There are no obligations to initiate pre-bankruptcy or extraordinary administration proceedings.
CY	If, during liquidation, a director is proved to be involved in fraudulent trading under Section 311 of the CCL or some other offence (such as misappropriation of assets under section 312 of the CCL), the court may make an order for him/her to be personally liable for the company's debts or to pay compensation. However, in the absence of severe misconduct such as this, there are no provisions for lifting the corporate veil.
CZ	The management of the debtor is under a duty to file an insolvency petition on behalf of the debtor without undue delay after it learns or with due diligence ought to have learnt about the debtor's insolvency. The management (the executives and directors) is personally liable for a failure to file the insolvency petition on time. The law gives a presumption that the damage that a creditor is entitled to recover corresponds to the entire unsatisfied portion of the creditors' claims. The liability is strict, and mitigation is possible only if the defendant proves that the delay had no adverse effect on the extent of the creditor's satisfaction or if the petition was not filed due to circumstances beyond the defendant's control.
DK	Once a company reaches the point-of-no-return, its management has an obligation to cease the operations of the company, ensure the equal treatment of creditors and initiate the necessary insolvency proceedings. If it is considered gross negligence on the part of management to allow a company to continue trading beyond the point-of-no-return, then management can be held liable for any losses suffered by creditors as a result thereof. Such a claim against management can be brought by either the trustee or an affected creditor. Also, if management is deemed to have grossly mismanaged its duties, it risks being put into bankruptcy quarantine – i.e., prohibited from participating in the management of any limited liability company for a given timeframe (usually three years).
EE	Members of the management board or of a body substituting for the management board are liable for

	the failure to submit a bankruptcy petition.
FI	The general duties of the board of directors and the managing director of the company (together the 'Management') are set out in the Companies Act (CA). According to the CA, the board of directors of a debtor company has a general duty of care towards the company's stakeholders (CA, Chapter 1, Section 8). In addition, the board of directors is responsible, together with the managing director, for ensuring that the company's accounting and financial affairs of the company have been arranged in accordance with the law and in a reliable manner (CA, Chapter 6, Sections 2 and 17). The managing director must provide information on the company's financial standing to the board of directors, which, in accordance with the general duty of care, shall assess the need to file for insolvency proceedings in the event of the company being in financial distress. Trading should be discontinued where continuing is likely to worsen the company's financial distress or cause insolvency. In addition, the board of directors has an obligation to act in case the shareholders' equity is adversely impacted (CA, Chapter 6, Section 2). When considering the interests of the company and its stakeholders, the company's management should also take into account the interests of the company's creditors to a certain extent. According to the CA (CA, Chapter 22, Section 1), members of the board of directors and the managing director may become personally liable for the loss or damage caused to the stakeholders by a delay or failure to file for insolvency. A member of the board of directors may be held personally liable for a wilful or negligent breach of the general duty of care or the company's articles of association. In a distressed situation, actions by the board of directors that diminish the assets or increase the liabilities of the company without a business rationale, are particularly susceptible to trigger liability.
FR	Liability can arise where, as a result of management errors, a company's assets do not cover its debts. An action for mismanagement (other than mere negligence), which only applies in liquidation proceedings, can lead to an insolvent company's management being liable for all or part of its debts. This liability can extend to formally appointed directors or managers with representation powers, and to any individual or entity that is not officially a director or manager but, that repeatedly influenced the company's management or strategic decisions (that is, shadow (de facto) directors/managers). In addition, directors (or de facto directors/managers) found liable for certain specific breaches can be (independent of any liability action or criminal prosecution based on the same facts): Forced to assign their equity interest in the company. Prohibited from managing any business for up to 15 years and holding any public office for up to five years. Breaches include: Using the company's assets or credit for their own benefit, or the benefit of another corporate entity in which they have a direct or indirect interest; Using the company to conduct and conceal business transactions for their own benefit; Carrying out business activities at a loss to further their own interests, knowing that this would lead to the company's insolvency; Fraudulently embezzling or concealing all or part of the company's assets; Fraudulently increasing the company's debts.
DE	If a company is insolvent, its managing director is generally not liable for the company's debts, with the following exceptions: Suretyship, guarantee, or other contractual obligation; Liability for payments made after illiquidity or over-indebtedness. A managing director will be liable towards the insolvency estate for any payments made by the company to third parties after the company has become illiquid or over-indebted (section 15b, GIC). The insolvency administrator (or in the case of self-administration, the custodian) can bring a claim against the managing director to recover the money paid. The background for this liability is that on illiquidity or over-indebtedness, the managing director must file an insolvency petition without undue delay (at the latest, three weeks after the commencement of illiquidity or six weeks after the commencement of over-indebtedness). The liability for payments made after illiquidity or over-indebtedness is subject to very limited, narrow exceptions; Liability for payments to shareholders resulting in illiquidity or over-indebtedness of the company; Delayed filing of insolvency petition. If a managing director fails to file an insolvency petition without undue delay, they are liable for both payments made after illiquidity or over-indebtedness and any decreases in insolvency quotas;

	Preservation of capital. A managing director is liable towards the insolvency estate for unlawful repayments of capital. Exceptions apply if the payment is made under a profit transfer agreement covered by a collectible claim for repayment against the shareholder or made in respect of repayment of a shareholder loan; Duties of care. A managing director is liable towards the insolvency estate if they fail to act with due care in managing the company's affairs. For example, a managing director must: comply with applicable laws, by-laws and articles of association (Satzung); ensure proper organisation of the company, including compliance of the company with applicable laws; carefully prepare all business decisions in advance, being aware of any risks, and of financial impact, and of alternatives, and compile the necessary documentation in advance (business judgement rule, as understood under German law). In practice, however, a defence based on the business judgement rule will often not be successful because one or more of the prerequisites can often not be proven because they were not fulfilled or documented in advance; supervise any developments which may jeopardise the company's survival. Embezzlement of company's assets; Tort. A person who, in a manner contrary to public policy, intentionally inflicts damage on another person or company is liable to the other person or company to make compensation for the damage; Tax debts. A managing director is liable to the tax authorities for any failure of the company to settle tax obligations when due, if they acted wilfully or through gross negligence; Employees' share of social security premiums. A managing director is liable to the social insurance authorities for any failure of the company to pay employees' share of social security premiums; Deception regarding illiquidity. A managing director is liable towards a contract partner if the contract partner (for example, a supplier) is deceived about the company's illiquidity.
EL	Specific duties are provided for under the Insolvency Code for the members of the board of directors. Failure to file (or delay in filing) for bankruptcy upon cessation of payments exposes the directors to personal liability. The same applies if bankruptcy results from gross negligence or wilful misconduct of the directors, while the directors are further exposed to criminal liability in the event of loss-making or extraordinarily risky transactions, inappropriate borrowings, misleading or incomplete company books and records, failure to prepare and approve financial statements or inventories as required by law, undue disposals or deterioration of assets, or preferential payments to the detriment of other creditors. Furthermore, the directors have personal and criminal liability in the event of tax indebtedness, in accordance with tax legislation.
HU	The liquidator or the creditors may lodge lawsuits against the debtor’s former directors for their activities which were detrimental to the interests of the creditors on the grounds that the former directors did not carry out their managerial functions, taking into account the creditors’ interests when a situation with the threat of insolvency arose, leading to a decrease in the economic operator’s assets, or frustrated the full satisfaction of the creditors’ claims or neglected to settle environmental charges. If this is proven, the former director of the debtor must compensate the creditors for the damage thus caused.
IE	Directors or officers can be liable for the debts of an insolvent company in the following circumstances: Reckless trading. Personal liability can arise if, in the course of winding up a company, it appears that any person was, while an officer of the company, knowingly a party to the carrying on of any business of the company in a reckless manner. Liability can also apply to directors who ought to have known that these actions were reckless; Misfeasance. Where it appears that a director or other party has misapplied the assets of the company or been guilty of ‘misfeasance’ or breach of duty or breach of trust, the court can compel him to restore such assets or to provide the company with compensation in respect of such misapplication of its assets. This provision is not confined to directors and officers of a company but applies to any person who has taken part in the formation or promotion of the company. It is also not limited to insolvent procedures; Fraudulent trading. Where a person is knowingly a party to the carrying on of a business with intent to defraud creditors of the company or any other person, or for any other fraudulent purpose, that person will be guilty of an offence; Failure to keep proper books and records. A director or officer of an insolvent company can be held personally liable for debts of the company where they have failed to keep proper books and records and where that failure has contributed to the company's inability to pay its debts as they fell due,

	caused uncertainty as to the assets and liabilities of the company, or has impeded the orderly winding-up of the company.
IT	There is no way that directors can be held liable for a company's debts. They are liable for personal debts arising from liability actions that can be brought against them by: The company, when directors are in breach of their fiduciary duties; The company's creditors, when directors are in breach of their duty to preserve the integrity of the company's assets to the extent that they are no longer sufficient to satisfy the creditors; A single shareholder and/or third party, whose personal assets were damaged by the directors' misconduct. Liability actions against directors are brought by the bankruptcy trustee, when the company is declared bankrupt.
LV	Directors must take care about safeguarding the assets for the creditors as well as timely apply for insolvency of the company. Additionally, both directors and any other responsible representative must be able to transfer the books and assets of the company to the insolvency administrator, should insolvency proceedings of the company be started. The directors who are management board members are jointly liable for losses caused to the company in case they fail to transfer the books to the insolvency administrator, or, if the condition of the books does not allow to obtain a clear understanding of the company's transactions and assets in the three years prior to the commencement of insolvency proceedings. The Insolvency Law contains a presumption that the losses are in the amount of the accepted principal claims of the creditors.
LT	In Lithuanian case law and doctrine, the general obligation to initiate insolvency proceedings in a timely manner is regarded as an imperative duty of the director, and failure to comply with this duty is unlawful inaction that may cause damage and therefore incur a director's civil liability. This is a clear element of the liability for delaying insolvency proceedings doctrine.
LU	Directors' duties in case of bankruptcy The managing director is declared negligent bankrupter if: their personal expenditure are deemed excessive, or; they have spent large sums of money in gambling, or in fictitious stock exchange transactions or with the intention of delaying their bankruptcy, they: made purchases to resell at a loss; or engaged in ruinous borrowing to raise money; or cannot justify the use of assets and funds; or if, after the cessation of payments, they have paid or favoured a creditor to the detriment of the pool of creditors. A managing director manager may also be declared negligent bankrupter if s/he: have contracted for the account of others, without receiving any value in exchange; are declared bankrupt, without having fulfilled the obligations of a previous scheme of composition; have not made an admission of cessation of payments within the time limit; have been absent without authorisation from the examining magistrate; have not kept their accounts in accordance with the law. Duties of Managers of Public - Limited Companies The managers of public limited companies (SA) may still be sentenced as a negligent bankrupter if they: do not provide the information requested by the examining magistrate or the trustee; or provide inaccurate information. Bankrupt of the managing director The managing director is declared fraudulent bankrupter if s/he: remove company accounts or other accounting documents, or fraudulently alter their content; or misappropriate or conceal part of their assets; or fraudulently acknowledge that they owe amounts that are not owed.
MT	If a director mismanages the company in a way that endangers the good governance of the company or fails to adequately supervise and act as the bonus paterfamilias while managing the company's affairs, he would be personally liable for the damages ensued by the company. Directors can be liable for the following acts under the MCA: Duty to file for insolvency; Fraudulent preference; Duty to keep proper accounting records; Fraudulent or wrongful trading.

	Article 329A of the MCA provides that where the Directors become aware that the company is unable to pay its debts or is imminently likely to become unable to pay its debts, they shall convene a General Meeting of the company to review the company's position and to determine the next steps that should be taken. Under MCA, any act which dispossesses the property or rights of the company made in the period of 6 months prior to the dissolution of the Company, shall be deemed as fraudulent preference against its creditors if it is made gratuitously or at an undervalue or if preference to any creditor is given. Directors may incur liability when proper accounting records are not kept by the insolvent company under Art. 314 of the MCA. Fraudulent trading is defined as carrying out acts with the intention to defraud: creditors of the company; or creditors of any other person; or for any fraudulent purpose. Under Maltese law, directors can be subjected to the following sanctions: Disqualification – under Art. 320 MCA, if the director is found guilty in terms of Section 312 (delinquent directors), (fraudulent trading) and (wrongful trading) and consequently ordered by the court to make a contribution to the assets of the company or declared personally liable for the debts of the company, is subject to a disqualification order; Liability in tort – direct liability if the director is involved in fraud or other crimes; Criminal liability; Administrative fines – for failure to inform the Registrar regarding a resolution for the dissolution and voluntary winding up of a company
NL	Only a few managerial duties are described in the Dutch law. An example is the standard of care that the director should observe towards the company. A director may be held liable by the company itself – or, in case of bankruptcy, by the trustee − for the damages suffered by that company when he acts contrary to his obligations and the damages are a result of that mismanagement. The director is obliged to perform to the best of his abilities in the interest of the company and as could be reasonably expected from a competent and qualified director under the same circumstances. For liability to be accepted there must be a serious personal reproach/fault on the side of the director. All relevant facts and circumstances must be taken in account. Not every imperfection or mistake leads to liability: the director is granted a certain degree of latitude. In principle, collective responsibility entails that all directors are severally and jointly liable for failure, although individual directors do have the opportunity to exculpate themselves when held liable. For exculpation the director must show that he is not to blame for the mismanagement and that he has not been negligent in taking measures to avert the negative consequences of the mismanagement. The board of directors may also be discharged by the general meeting of shareholders, lifting the directors from (internal) liability with regard to the management in the period relevant to the discharge. The discharge only relates to the facts that are officially known to the general meeting. An example of improper performance is entering into irresponsible financial transactions involving great financial risks. Another example of internal liability may apply when a director forces a company to lend a large amount to a third party without stipulating security and/or interest and the third party subsequently goes bankrupt.
PL	Directors are responsible for any damage caused as a result of their failure to file a petition within the applicable time limit, unless they are not at fault. It is presumed that this damage covers the amount of unsatisfied creditor receivables toward the company. Members of the management board may also be subject to specific liability consisting of a prohibition on holding managerial positions or conducting business activity for a period of 1 to 10 years in the case of, inter alia, a wilful failure to file for bankruptcy in the event of the company's insolvency.
PT	Directors are also legally required to apply for a declaration of insolvency on behalf of the company within 30 days of the date on which directors become aware of, or ought to have become aware of, the insolvency situation
RO	There is liability for wrongdoing committed before the proceedings are opened. Corporate officers and directors are personally liable if they have committed one of the following acts, if it resulted in the insolvency: they used the goods or credits of the legal person for their own benefit or for that of another person; they carried out the activities of production, trade or provision of services in personal interest, under

	the cover of the legal person; they ordered, in personal interest, the continuation of an activity that obviously led the legal person to the cessation of ayments; they kept fictitious accounts, made some accounting documents disappear or did not keep the accounts as required in accordance with the law. In the case of non-delivery of the accounting documents to the judicial administrator or the judicial liquidator, both the fault and the causal link between the deed and the damage are presumed, the presumption being relative; they have misappropriated or concealed a part of the legal person's assets or have fictitiously increased its liabilities; they used ruinous means to procure funds for the legal person to delay the cessation of payments; in the month preceding the cessation of payments, they have paid or are willing to pay in a manner that favours one creditor to the detriment of the other creditors; or any other deed committed intentionally that contributed to the debtor's state of insolvency, as ascertained according to the provisions the law.
SK	In general, directors are liable for damage caused to the company as a result of a breach of their duties, whether in cases of financial distress or not. For the liability to arise there has to be: a breach of a duty under the law or incorporation documents of the company; damage incurred by the company; and a causal link between the breach and the damage incurred by the company. A breach of duty can be based on a director's action or omission. The breach does not require a culpable act (i.e. negligence or intent of a director). The law provides for a rebuttable legal presumption that a director has breached their duties. This means that unlike in standard damage claims, where the claimant would bear the burden of proof regarding the breach, in the event of a breach of duties the burden of proof rests on the director, who must substantiate that the duties were not breached. There are several legal provisions that create directors' liability in the case of financial distress. For instance, if a director found out or, considering all circumstances, could find out that the company is in crisis (i.e. if the company is insolvent or at risk of insolvency), the director is obliged to procure all reasonably necessary steps to overcome the crisis. Further, directors may not distribute dividends or other distributions to shareholders if, considering all circumstances, it causes insolvency of the company and the company's equity to be lower than its share capital plus reserve funds. Furthermore, there are a number of other cases of specific personal liability of directors which are discussed in the following parts of this survey
SI	When a company becomes insolvent management must, within one month, draft a report on its financial position and its opinion of its chances of restructuring and, based on this report and the likelihood of successful restructuring, either financially restructure the company or petition for bankruptcy (after which, the supervisory board must opine on such report within five working days). If the management or the supervisory board of the company fails to fulfil their respective duties, their individual members will be jointly and severally liable to the creditors for any damages incurred by the creditors due to the members' failure to achieve complete payment in bankruptcy proceedings. The ZFPPIPP provides specific rules on damage liability, amount of damages, exemptions and limitations of the liability, enforcement of claims and more.
ES	The failure to take reasonable steps to minimise losses to creditors may violate the duties and responsibilities of directors. Article 164(1) of the Insolvency Act provides that the insolvency will be found to be negligent when the insolvency has been originated or aggravated with bad faith or gross negligence on the part of the company's directors or liquidators (or any person holding such a position in the two-year period before the filing of the insolvency petition). If the insolvency is found to be negligent, the directors can be held liable for 'bankruptcy liability', that is the liability to cover the deficit between the assets and the liabilities. In addition, if directors violate their duties by misappropriating corporate assets, the insolvency will be declared negligent, and the directors would be subject to bankruptcy liability. Article 164(2.4) of the Insolvency Act provides that the insolvency will be found to be negligent when the debtor has taken all or part of his assets to the detriment of his creditors, or had carried out any act that delays, makes difficult or impedes the efficiency of a seizure of assets in any kind of enforcement action.
SE	Where there is reason to believe that the shareholders' equity is less than one-half of the registered share capital or if it has been shown during execution of a distraint order that the company lacks attachable assets, the board of directors is obliged to prepare immediately a balance sheet of the company for liquidation purposes.

	Directors must issue a notice of a general meeting if the balance sheet shows that shareholders' equity is less than one-half of the registered share capital. If a second balance sheet, prepared within a set time limit, shows that the shareholders' equity still does not exceed one-half of the registered share capital, the board of directors has a duty to petition the court for a liquidation order. Should the board of directors fail to prepare the balance sheet (to convene the initial general meeting) or to petition the court for a liquidation order within set time limits, the directors can be jointly and severally liable for the obligations incurred by the company during the period of such failure to act, unless a director can prove that he or she was not negligent.

Source: Deloitte/Grimaldi (2022).

2.4 Pre-packs

Piece-meal asset liquidation of the insolvency estate or its restructuring or reorganization, usually in the form of sale of businesses in insolvency on "a going concern basis", including pre-package sales ('pre-packs'). A sale on a going concern basis means a liquidation of a debtor by the sale of the whole or a significant part of the business as an operating and functioning entity as opposed to the so-called piece-meal liquidation under which individual assets of the business are sold separately. The opposite of this approach of transferring assets is the so-called piece-meal liquidation, consisting of a sale in which "individual assets of the business are sold separately", a sale that may come into play in the event of a business liquidation.

A pre-pack sale means a sale on a going concern basis under a contract which is negotiated confidentially prior to the commencement of an insolvency procedure without consultation of all creditors and followed by a very short formal insolvency proceeding in which the pre-negotiated sale and settlement is confirmed.

A 'pre-pack' describes a sale of all or part of the business, negotiated before filing for insolvency and in secrecy, followed by a liquidation procedure where the court quickly distributes the proceeds from the sale to the creditors. The availability of a pre-pack procedure maximises value preservation in the sale as a going concern, which tend to result in a much higher price being paid by a purchaser than sales on a break-up or piecemeal basis[299].

Usually, there are two methods based on which the transfer of business activities takes place, i.e. either by transferring the shares of the company running the business, or by selling the entire business or a substantial part thereof (a substantial part of the assets, including contractual positions and liabilities, goodwill, etc.). The transfer of a business or a business branch can also be used as a tool for restructuring or reorganising the business[300]. The purpose of such a transfer would be to keep the business running, by

[299] U.S. Congressional report on the measures that led to the US Bankruptcy Code makes the common sense point that "assets that are used for production in the industry for which they were designed are more valuable than those same assets sold for scrap" HR Rep No 595, 95th Congress, Ist Sess 220 (1977).

[300] UNCITRAL uses the term reorganization as well, to which the following definition applies: "*a reorganisation is the process whereby the financial well-being and viability of a debtor's business can be restored and the business can continue to operate, using various means possibly including debt*

separating the activities, that can still be profitable, from the debtor while the latter shall be left with those activities that are not viable anymore.

Through a prepack, the sale of the business (as a going concern) will take place at the very start of the proceedings, right (or very shortly) after the opening of the formal liquidation proceedings. This can be achieved, because the complete preparation of the actual business sale (i.e. the marketing of the business and the negotiation with the possible buyer) takes place – usually in a confidential manner – before the formal opening of the proceedings, under the steering of a 'silent administrator'.

The procedure consists of an accelerated winding-up procedure, which allows for the sale of the debtor's business (in whole or in part), as a going concern, to the highest bidder selected during a competitive sale procedure ("preparation Phase") preceding the formal opening of the liquidation ("winding-up Phase")[301]. This liquidation procedure is without prejudice to the other aspects of the insolvency law, i.e. the ranking of claims and distributional rules, that continue to apply as long as they are compatible.

The 'prepack procedure' is considered a liquidation procedure and is acknowledged under Annex A of EIR. Furthermore, based on Council Directive 2001/23/EC of 12 March 2001, the pre-pack is also considered as a bankruptcy or insolvency procedure initiated with a view to liquidating the assets of the transferor under the supervision of the competent public authority. In the context of bankruptcy practice in Europe, sales on a going concern basis were already regulated in several Member States already in 2003[302]. These sales on a going concern basis are governed differently in different Member States depending on whether or not bankruptcy law prevails and, therefore, whether or not the sale of an asset takes place in the context of formal insolvency proceedings.

Pre-packs sales are a fast and efficient way to recover value for creditors/investors. They can increase the recovery value by selling parts of the defaulting company early on, thereby reducing the deterioration of the asset values. While the instrument seems most commonly used to restructure a company and spin of the viable from unviable business lines, they can also play a useful role in liquidations.[303] There may still be business lines that are viable and assets that worthy, so their early realisation and transfer in a package could maximise the recovery value.

Unlike in a restructuring case, the position of the debtor should not matter if a pre-pack is used during the winding down of the company. All creditors should benefit from the

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forgiveness, debt rescheduling, debt-equity conversions and, our focus in this chapter, sale of the business (or parts of it) as a going concern".

[301] ELI Instrument – *Rescue of Business in Insolvency Law*, cit., Recommendation 7.03.

[302] The principles of European insolvency law (2003) under Section 12.1 provide that: *"If and to the extent that there is no reorganisation, the administrator converts the debtor's assets into money and distributes it among the creditors. The assets can be realised separately or together, whether or not as a going concern".* The Leeds Study (2016) lists France, the Netherlands, Greece, Ireland and Slovenia and the ELI 2017 Instrument 'Rescue on Business in Insolvency Law' adds Germany and Italy to the list.

[303] Schoenfeld (2020) found however that the financial situation is an important determinant of consent on pre-packs and financial performance tend to be poor in an analysis of restructuring cases in the Czech Republic.

higher recovery value realised through pre-packs. The survival of individual business lines as going concern would also be in the interest of other stakeholders such as employees or public authorities. Smaller and also foreign creditors may however be concerned that larger and domestic creditors will have a key role in determining the conditions under the pre-pack takes place, possibly even taken over viable business lines or assets at a price favourable to them.[304] Foreign creditors may see themselves disadvantaged if rules governing the pre-pack are non-transparent and accountability is unclear. Comparable rules on pre-packs would be to their advantage and could encourage their cross-border lending activity.

Pre-packs are build on the insight that there is likely to be a substantial saving of cost and convenience if a debtor minimises the time that it spends in formal insolvency procedures. The longer and more drawn out the procedure, the greater the costs and expenses that are likely to be incurred. Further to the sales on a going concern basis another instrument may be envisaged in cases where there is a risk that the value of the debtor's assets will decrease significantly in a short period of time[305], i.e. the prepack sales. In events where there are situations such as to ensure that the direct appointment is not detrimental to creditors' interests, Member States may either allow debtors and/or creditors (or creditors' committees) to directly choose the advisor without the involvement of a court or allow the insolvency practitioner to directly authorise and execute the sale of the assets without the involvement of a court.

Member States shall ensure that insolvency practitioner participating in pre-pack procedures have relevant experience and expertise, retain liability in case of failure to perform their duties and receive appropriate remuneration, proportionate to their potential responsibilities[306]. On the other hand, the Court shall have exclusive jurisdiction over any dispute arising in the course of the pre-pack procedure, any action against the advisor subsequently appointed as the insolvency practitioner and over urgent operational measures that may be instrumental to the success of the pre-pack procedure, such as termination or amendment of employment agreements. Member States shall ensure that, during the preparation phase, the pre-pack applicant should be entitled to apply for a stay or moratorium of enforcement measures[307] also in order to facilitate the Pre-pack procedure and provided that the advisor approves such an application for a stay.

The 2019 Directive on Restructuring and Insolvency lists the sale of the business as a going concern as one of the measures of ‘restructuring’, but this is just offered as an option for Member States, depending on their laws, and is not harmonised. Furthermore, in the preventive restructuring framework such a sale forms part of the restructuring plan and the legal entity usually is kept (is not liquidated). The pre-pack liquidation procedure is, therefore, a new solution, for which there is a demand on the side of the stakeholders.

[304] These points are also made as major disadvantages of pre-packs in Cormack et al. (2016).
[305] ELI Instrument – *Rescue of Business in Insolvency Law*, cit., Recommendation 7.02.
[306] ELI Instrument – *Rescue of Business in Insolvency Law*, cit., Recommendation 7.04.
[307] As provided for in Articles 6 and 7 of Directive 2019/1023

Table A5.5: Prepack rules and practices in the EU Member States

AT	Under the new draft legislation[308] (entered in force in July 2021), Austria will implement the pre-pack sales via a 'simplified' restructuring plan proceeding. According to the draft, the debtor agrees the restructuring measures (potentially including sale of assets/business and debt cut) and – together with the required majority of financial creditors – applies for the court's approval of the restructuring plan.
BE	Not existent. But the Business Continuity Act (BCA) of 2009 provides debtors in a state of financial crisis with three tools apt to reorganise their business, i.e.: (i) an amicable settlement; (ii) a collective reorganisation plan or (iii) a transfer of the enterprise or of its activities, in whole or in part, to third parties under court supervision (Leeds)
BG	Not existent.
HR	Pre-bankruptcy agreement exists and operates in a reversed manner – pre-bankruptcy court proceedings are opened and aim at the conclusion of a pre-bankruptcy settlement with the creditors outside of bankruptcy proceedings, which will enable the reorganisation of the debtor. However, the court is involved – it verifies whether the conditions for confirmation of pre-bankruptcy arrangement have been met.
CY	Pre-packaged sales are not common in Cyprus though they may be implemented through receivership.
CZ	The option of pre-packed insolvency ('*pre-pack'*) is perceived as a fast and effective way of reorganisation in the Czech Republic. Reorganisations, in general, are subject to the size and other constraints set out in Section 316 Article 4 of the Czech Republic Insolvency Law (CRIL). The pre-pack is the only case in which these criteria do not have to be met, which means that the reorganisation procedure is also open to SMEs when their creditors agree with the rehabilitation procedure and a suggested reorganisation plan. The pre-pack prepares the ground for further derogations in distressed companies' behaviour and has the advantage that the creditors already agree with the suggested reorganisation plan before the insolvency proposal. This avoids the negotiation processes during the insolvency proceedings and can potentially shorten the insolvency proceedings and achieve other positive effects.
DK	Pre-packed sales are allowed, but the trustee must ensure that the sale is made on arm's-length terms.
EE	No information
FI	Not existent. Distressed debtors and their creditors may enter into voluntary contractual agreements out of the court proceedings. However, the contract must focus on debt restructuring (ex: extending the repayment period or cutting the outstanding amount).
FR	The law of 22 October 2010 on banking and financial regulations, effective as of 1 March 2011, and its implementing decree of 3 March 2011, created a type of accelerated safeguard inspired by the US Chapter 11 pre-pack. The purpose of this expedited financial safeguard process (*sauvegarde financière accélérée*) is to restructure financial debt in a very short time frame, assuming the consent of at least two-thirds of financial creditors and of bondholders.
DE	Not existent *per se*. So-called prepacked plans in a German context are insolvency plans that are planned and created before the debtor files a request for insolvency. Usually, they are submitted together with the petition to open insolvency proceedings.
EL	Pre-packs business recovery process is available contingent to court ratification
HU	Not existent.
IE	The usage of pre-pack insolvency sales is less developed in Ireland than in other jurisdictions, but there has been an increasing number of asset sales structured through pre-pack receiverships. In Ireland there are no corresponding rules or guidelines in general usage, although some insolvency professionals follow the Statements of Insolvency Practice guidelines. In the absence of detailed rules, the critical standard for the appointed insolvency office holder is to ensure that he obtains the best price possible for the assets at the time of sale. Provided the insolvency office holder complies with this test and adheres to the highest professional standards, there is no barrier to effecting a pre-pack sale in a manner which stands up to scrutiny and which will allay the concerns of creditors.

[308] The Restructuring Code (Restrukturierungsordnung).

IT	Pre-packed plans provide for the sale or lease of the debtor's assets to a third-party investor, based on agreements reached by the debtor and the third-party investor prior to filing. Should the assets be sold to a third party different from the original investor as a consequence of the competitive procedure above mentioned, the latter has the right to be reimbursed for the costs incurred in connection with the agreement reached with the debtor up to an amount equal to three per cent of the price of the assets agreed therein.
LV	No information available
LT	There are no pre-pack sales identified in the Lithuanian law
LU	No information found.
MT	Pre-packs are not formally codified under Maltese law, and practice has thus far not necessitated their judicial recognition. However, the local legislative architecture may indeed be stretched to accommodate pre-packs; if pre-packs were to enter into vogue locally as a result of developments in the Maltese restructuring market, they could be sanctioned under the CRP or the compromise or arrangement restructuring route. Since pre-packs thrive on speed of execution and minimal court involvement, the CRP would seem to be the more appropriate route for their execution. Where all required consents to the pre-pack are solicited before entry into the CRP, the issuance of the company recovery order (approving the pre-packaged sale) may take place shortly after, and, in any event, within a maximum of 20 days of the CRP application being filed. There would be no plausible grounds for a putting a pre-packaged restructuring plan to creditor or member meetings and subsequently applying to the courts to sanction its outcome under the compromise or arrangement option, unless such option is necessary to overcome hold-out within an impaired debt tranche.
NL	In Netherlands there is the option of a pre-packaged bankruptcy filing. Before filing for bankruptcy or suspension of payment, the company's management, shareholder or (third party) investor and/or purchaser prepare a plan to acquire or sell certain parts of the business out of the (bankrupt) estate and continue business in another company standing at the ready. Following the preparation of such plan, the court may be asked to appoint a '*silent administrator*' prior to the request for bankruptcy (or suspension of payment) to ensure that the pre-pack plan is acceptable to the administrator and the bankruptcy judge.
PL	A debtor that has become insolvent can also find a buyer for its assets on its own. The debtor can then file a bankruptcy petition along with an application for approval of the terms of sale of the enterprise—known as a 'pre-pack.' It is also possible to file a pre-pack application after filing of the bankruptcy petition. A pre-pack application may also be filed by an *in personam* creditor of the debtor. A pre-pack consists of a sale of the assets of an insolvent debtor, approved by the court, but negotiated and prepared prior to the declaration of the debtor's bankruptcy. This procedure allows an investor to quickly acquire the assets of an insolvent company, relatively soon after the declaration of bankruptcy, unlike the time-consuming acquisition of assets under the standard conditions of bankruptcy procedure. In the pre-pack procedure, it is possible to acquire the debtor's enterprise, an organised part of the enterprise, or a set of assets constituting a significant portion of the enterprise. A sale made in the form of a pre-pack has the effects of a sale in execution (acquisition free of encumbrances on the assets or debts of the debtor).
PT	There are no pre-pack procedures.
RO	Pre-pack administrations are not regulated under Romanian law. The sale of assets in distressed M&A transactions is stricter once the target has entered insolvency. Insolvency proceedings are highly regulated under Romanian law, and involve various approvals and confirmations that must be obtained from the creditors' assembly and the court of law prior to implementing it: In case of bankruptcy, the assets will be evaluated by an authorised valuator and the creditors committee must approve the valuation reports as well as the type of sale (direct negotiation, auction or a combination of the two) and the sale regulation.
SK	There are no rules concerning pre-pack sales in Slovakia
SI	Pre-package sales are not foreseen by Slovenian law. [some use according to Leeds]
ES	For the time being, there is no specific legal regulation of this figure in the Spanish legislation. But from the actions already carried out, the following structure can be observed: First, there is a preliminary phase. During this phase, the entrepreneur must inform the Court of the opening of negotiations with its creditors. Then, it must communicate that operations are being carried out regarding the sale of production units. An independent expert appointed

	by the company will be in charge of carrying out the sale of the production units. This independent expert will also be in charge of ensuring compliance with the law and providing transparency to the process. Once the insolvency proceedings are declared, this independent expert will become the insolvency administrator. The second phase is the judicial phase of authorization and implementation of the pre-pack operations. This will be done through Article 530 of the Consolidated Text of the Insolvency Law. This determines that the debtor must present a liquidation plan with a proposal for the acquisition of the productive unit. Subsequently, the judge will agree the opening of the liquidation phase.
SE	Pre-packaged sales are possible in practice and is not uncommon. However, a pre-pack and its commercial terms will always be reviewed by the official receiver in subsequent bankruptcy proceedings, thus with a risk of being set aside. Also, with little transparency and no creditor consultation pre-packs have been debated, and still are, especially where the business/assets are sold to someone connected to the debtor. When doing a prepack sale, it is recommended to obtain a third-party valuation of the property sold, to avoid a sale at undervalue which can be criticized and potentially challenged.

Source: Deloitte/Grimaldi (2022).

3. Procedural elements of insolvency

3.1 Opening of insolvency

Under insolvency frameworks of Member States there are different understandings and definitions of when a business should be obliged to undergo insolvency proceedings. Systems diverge considerably between Member States that equate insolvency with illiquidity (inability to pay debts when they fall due) and Member States which (in addition also) consider a company insolvent if it is over-indebted on the basis of a balance sheet analysis.

There are typically two insolvency tests under national law to kick off an insolvency proceeding: cash flow (i.e. a company cannot pay its debts as they become due) and balance sheet (i.e. the value of a company's liabilities outweigh the value of its assets). In practice it is, however, not easy to determine whether either or both of these tests are satisfied. What often causes difficulties is how one deals with contingent and prospective liabilities and assets. That means that in reality there could be as many as 27 different answers to the question of whether a business is (in)solvent.

In practice, however, it is often not easy to determine whether the opening of the insolvency test requires that either or both of these tests need to be satisfied. According to UNCITRAL, insolvency occurs "when a debtor is generally unable to pay its debts as they mature or when its liabilities exceed the value of its assets"[309]. This can happen due to a company making a bad investment, misjudging business risk, or making mistakes in pricing. However, general market changes or an economic downturn can also drive a company to insolvency. Thus, the reasons that in the abstract can lead to a situation of insolvency can be both internal (for instance bad management of funds) to the company and external (for instance disruptive change in the markets).

The 2019 Restructuring and Insolvency Directive leaves it up to Member States whether they wish to require that companies seeking the advantages of a restructuring (including a

[309] Uncitral, United Nations Commission on International Trade Law, Legislative Guide on Insolvency Law, 2005.

moratorium on debt payments) need to undergo a viability test to determine whether a restructuring is likely to have more than short-term effects and to avoid 'zombie' companies. It was not possible to agree on a mandatory viability test in the 2019 Restructuring and Insolvency Directive, let alone define what it should look like. This Directive is now being transposed by Member States (many of which requested an extension of the transposition deadline by July 2022).

In a competitive economy, companies that are not economically viable (e.g. because their business idea has lost its appeal to the market) should exit the market to allow for the re-attribution of resources to more innovative companies. One avenue to ensure the timely initiation of insolvency proceedings could be to explore a common definition of the prerequisites when insolvency proceedings should be commenced. It needs to be noted however that so far it has been considered too difficult to bring about a harmonisation of the notion of insolvency or likelihood of insolvency and even the European Insolvency Regulation determining international jurisdiction and the applicable law in insolvency matters refrains from such a common definition. Also it could be explored to which extent the information on the insolvency trigger should be made available in an investor-friendly format on e-Justice portal (see below). This would contribute to the investor's ex-ante awareness of the insolvency proceeding, allowing her/him to factor this in the cost of capital.

The pronounced differences in insolvency triggers across Member States imply learning costs for foreign creditors. These are likely higher the more discretionary and less explicit the trigger is defined and the more different definitions and concepts are in the destination of the investment from the location of the investor. A well-defined trigger reduces uncertainty to creditors and in particular to foreign investors, who would have lower learning costs if triggers are similar or based on a common terminology.

Creditors may face disadvantages from a well-defined trigger if they are accountable to ultimate investors and/or supervisors and therewith under pressure to correct their asset valuations once the trigger is reached. Such loss of discretionary judgment may however be beneficial for ultimate investors and financial stability. Debtors would benefit from clarity primarily in the run up to insolvency. A clear trigger would augment the debtors' problems once the threshold is reached because it inflicts reputational damage and will in many cases cut off the company from new financing. This accelerates the need to wind down the company and takes away any possibility that it can remain a going concern.

The setting of a clear trigger for the start of the process that leads to the liquidation of the company may however reduce the impact of such reputational effects in the pre-insolvency phase. In the presence of a well-defined trigger, both creditor and debtor would be able to assess under which conditions an insolvency process starts, which should create incentives for debtors to react pre-emptively as well as for creditors to seek solutions before courts get involved. This helps avoid that the start of an insolvency procedure is postponed, which means the beginning of protective measures (avoidance actions, treatment of all creditors), use of outside expertise (insolvency practitioners, viability assessment), initiates the search for a definite solution (creditors committee). Since the insolvency triggers have a direct impact on the opportunity of debtors to access appropriate tools preserving the value of their business or ensuring an orderly exit from

the market, divergences in laws obviously influence the performance level of the insolvency frameworks.

Table A5.6: Insolvency triggers in EU Member States

AT	The commencement of any proceeding under the Austrian Insolvency Act (AIA) is dependent on the existence of certain factual predicates. In the case of corporate entities, these are: illiquidity (cash flow insolvency or zahlungsunfähig; Sec 66, para 1 of the AIA); over-indebtedness (balance sheet insolvency or *überschuldet*; Sec 67, para 1 of the AIA).
BE	The two conditions for opening insolvency proceeding are: (i) the persistent failure to pay its debts, and; (ii) the company has lost the confidence of its creditors (Art. XX.99 BCEL). A company is deemed to have generally lost all creditworthiness when it can show that it cannot receive credit on the market (typically with financial institutions) at reasonable conditions for an amount that is sufficient to pay the company's debts as they fall due.
BG	There are two triggers for insolvency proceedings: (i) insolvency (inability to pay), and; (ii) over-indebtedness (of a limited liability company, a joint-stock company or a limited stock partnership). These triggers are not cumulative. Insolvency and over-indebtedness are objective factual conditions, which have legal definitions in the Bulgarian Commerce Act (BCA). Under Art 608 of the BCA, insolvency is assumed when the debtor has stopped his payments and may be present when the debtor has paid or is in position to pay partially or in full only the claims of individual creditors. According to Art 742 of the BCA, a trade company shall be deemed overindebted, provided its assets are insufficient to meet its financial liabilities
HR	Insolvency incurs when a debtor: (i) becomes insolvent (incapable of payment), or; (ii) becomes over-indebted. A debtor shall be deemed insolvent (incapable of payment) if, in the Register of the order of priority of payment liabilities kept by the Croatian Financial Agency, it has one or more registered unsettled liabilities, due for more than 60 days, for which there is a valid basis for payment. A debtor is considered to be over-indebted if the value of his assets does not cover the existing obligations.
CY	According to Cyprus Company Law (CCL), a company will be deemed to be insolvent if (i) the company fails to pay for more than 3 weeks a debt of more than five thousand euros, or; (ii) the company fails to execute in full a judgement/order/decree given by the court in favour of a creditor of the company, or; (iii) the court is satisfied that the company is unable to pay its debts as they become due, taking into account the company's future or possible obligations, or (iv) the court is satisfied that the value of the company's assets is less than its debts, taking not account future or possible debts.
CZ	A debtor is insolvent if *(these are cumulative conditions)*: (I) the debtor has multiple creditors; (ii) the debtor has pecuniary liabilities that are more than 30 days overdue; (iii) is not able to perform those commitments.
DK	Pursuant to the DBA, a debtor is insolvent when it is unable to meet its liabilities as and when they fall due, unless such inability must be deemed to be only temporary. The final decision is based on an assessment of the debtor's liquidity (a cash flow test). The fact that the debtor's liabilities exceed its assets is not generally of importance.
EE	The first main precondition for the opening of bankruptcy proceedings is the fact that the debtor is insolvent. A debtor is insolvent if the debtor is unable to satisfy the creditors' claims and, due to the debtor's financial situation, that inability is not temporary.
FI	The Finnish Bankruptcy Act provides that a debtor who cannot repay his or her debts can be declared bankrupt
FR	Judicial liquidation proceedings are opened when the business has reached the stage of cessation of payments and when judicial reorganisation is clearly impossible.
DE	The general reason for opening insolvency proceedings is inability to pay. There is inability to pay if a debtor is not in a position to meet payment obligations that have fallen due; insolvency is presumed as a rule if the debtor has stopped payments (Section 17(2) of the German Insolvency Code - GIC). If the debtor is a legal person or a company in which none of the partners is a natural person with unlimited liability, proceedings may also be opened on grounds of over-indebtedness. There is over-indebtedness if the debtor's assets no longer cover the existing liabilities, unless it is highly likely in the circumstances that the enterprise will continue in being for the next 12 months (Section 19(2) GIC)
EL	Under the Insolvency Code, bankruptcy proceedings commence by a declaration of the court on the

	application of any creditor, the debtor or the attorney general, if the debtor has ceased payments in the sense that it is generally and permanently unable to pay its debts as they fall due. In respect of simplified bankruptcy proceedings, cessation of payments is deemed to have occurred if the debtor does not pay the due amounts towards the state, the social security funds or credit or financial institutions for an amount of at least 60 per cent of the total amount due and for a period of at least six months, and if the non-performing debt or debts exceed in aggregate the amount of €30,000.
HU	The court will declare that a debtor is insolvent and order the liquidation proceeding, when: (i) the debtor has not repaid or disputed (in writing) an acknowledged or undisputed debt, arising out of contract, within 20 days of the debt's maturity and upon a subsequent written payment demand from the creditor; or (ii) the debtor failed to repay its debt within its maturity as stated by the court's definitive judgement; (iii) judicial enforcement proceedings against the debtor were unsuccessful; (iv) the debtor has breached the obligations it has undertaken under a composition entered into with its creditors in previous bankruptcy or liquidation proceedings; (v) the court terminated the previous bankruptcy proceedings; (vi) in the proceedings initiated by the debtor or the liquidator, the debts of the debtor exceed his assets, or the debtor could not or will not be able to satisfy his debts (debts) at the due date, and in the proceedings initiated by the liquidator, the members (owners) of the debtor business organization do not declare their commitment to provide the resources necessary for the payment of debts.
IE	The primary condition for opening personal insolvency proceedings is that the debtor is insolvent, i.e. they are unable to meet their debts as they come due. The nature and extent of the debts and the debtor's income then determines which of the three arrangement types is appropriate: DRN, DSA or PIA.
IT	The objective prerequisite for the declaration of bankruptcy is the state of insolvency provided for in Art. 5 of the Italian Bankruptcy Law (IBL), which establishes that a person is in a state of insolvency if he is unable to regularly meet his obligations. Insolvency can be manifested by defaults or other external facts (e.g. the escape of the entrepreneur or the closure of the premises in which he exercised the activity), which demonstrate that the debtor is no longer able to meet his obligations. An entrepreneur who can only partially pay his debts is considered insolvent, as is an entrepreneur who can fulfil his obligations, but only after they have expired, or in an irregular manner (e.g. an entrepreneur who is forced to sell real estate to satisfy the company's creditors).
LV	The insolvency proceedings of a natural person may be applied to a natural person who has been the Republic of Latvia for the last six months and who has financial difficulties (signs of insolvency): (i) There is no possibility of settling debts of a total of more than EUR 5000 for which the deadline has entered into; (ii) on the basis of verifiable circumstances, it will not be possible for that person to settle debts above EUR 10 000 for which the deadline is set to expire within one year.
LT	Bankruptcy proceedings may be brought against a legal person where the court has determined the existence of at least one of the following circumstances: (i) the company is insolvent; (ii) the company is late in making payments relating to employment relationships to its employees; (iii) the company is or will be unable to meet its obligations. In addition, company insolvency is understood to be a state where a company is unable to meet its obligations (does not pay debts, does not perform work paid for in advance, etc.) and the overdue obligations of the company (debts, overdue work, etc.) exceed one half of the book value of its assets.
LU	According to the law of Luxembourg, the conditions needed to open an insolvency proceeding are: (i) Status of trader ; (ii) cessation of payments: it means that unquestionable debts due for payment (e.g. wages, social security, etc.) are unpaid, with term or contingent debts and natural obligations not being sufficient; (iii) loss of creditworthiness (the trader can no longer obtain credit from banks, suppliers or creditors).
MT	Insolvency Proceedings (Companies) conditions: according to article 214(2)(a)(ii) of Chapter 386 of the Companies Act (MCA), the company shall be deemed to be unable to pay its debts: (i) if a debt due by the company has remained unsatisfied in whole or in part after twenty-four weeks from the enforcement of an executive title against the company by any of the executive acts specified in article 273 of the Code of Organization and Civil Procedure; or (ii) if it is proved to the satisfaction of the court that the company is unable to pay its debts, account being taken also of contingent and prospective liabilities of the company.
NL	A debtor who is in a situation where he has stopped to pay his due and demandable debts shall be declared bankrupt by court order, rendered either upon his own request or upon the request of one or more of his creditors. Moreover, the bankruptcy order may also be rendered for reasons of public

	interest or upon the request of the Public Prosecution Service. In practice this means, although not formally required, that such creditor must not only submit his own claim(s), but he has to make plausible as well that the debtor is in default of performing at least one other claim of another creditor ('supporting claim'). Only then the court is able to asses that the debtor has stopped to pay his due and demandable debts. So it is not possible for a creditor to lodge a petition for bankruptcy when the debtor only fails to comply with this creditor's claim(s). In such event the creditor can only try to acquire an enforceable judgment against the debtor (to be obtained after normal proceedings) which makes him entitled to foreclose the debtor's property, from which he, subsequently, may recover his claim(s).
PL	The Bankruptcy Law identifies two independent grounds for the existence of a state of the debtor's insolvency, known as the liquidity test and the balance-sheet test. ad 1: The essence of the liquidity test, which is the most common grounds for insolvency, is the debtor's loss of the ability to perform its monetary obligations as they come due. The Bankruptcy Law provides for a presumption that the liquidity test is met if the debtor's delay in performing monetary obligations exceeds three months. Ad 2: The balance-sheet test provides, in turn, that a debtor that is a legal person, a commercial partnership, or other organisational unit (with certain exceptions) is also insolvent when the value of the debtor's monetary obligations exceeds the value of the debtor's assets over a period exceeding 24 months.
PT	Insolvency is a factual situation of insufficiency of assets of any legal subject (insufficiency which translates into the impossibility to comply with its due obligations) described by the Insolvency and Recovery Code (Código da Insolvência e da Recuperação de Empresas – CIRE). In other words, insolvency is characterised as the impossibility to comply with the generality of the due obligations of an individual or legal entity, and this situation may be current (incapacity to comply with the due obligations) or imminent (situation of potential incapacity to generate cash flow to cover the liabilities).
RO	Any company is entitled to petition for insolvency in Tribunal as soon as it determines that it is/soon will be unable to perform payment of its current/or future debt exceeding the threshold of RON 50,000 (approx. EUR 10,000). At the same time, any creditor of a company may file an insolvency petition in court if its receivables against that company exceed the aforementioned threshold and are overdue for more than 60 days. The debtor may defend against the creditor's petition indicating that even if the above conditions are met, it has sufficient liquidity. In certain cases, the court may decide to oblige the petitioning creditor to pay a bond of up to 10% of the value of his claim (but not exceeding the sum of RON 40,000 equivalent EUR 8,000) in order to cover any damages incurred by the debtor in case the creditor's petition is without sufficient grounds.
SK	Insolvency means that the debtor has excessive debt or is cash-flow insolvent. A debtor has excessive debt if the debtor is obliged to keep accounts in accordance with the applicable legislation (Act No 431/2002 on accountancy), has more than one creditor, and the value of the debtor's liabilities is greater than the value of the debtor's assets. A legal person is cash-flow insolvent if it is more than 30 days overdue with the payment of two or more financial liabilities to more than one creditor. A natural person is cash-flow insolvent if he or she is unable to pay at least one financial liability 180 days after payment was due.
SI	Insolvency is defined as a situation where: (i) the debtor has been insolvent for a lengthy period of time because it was unable to pay all of its obligations due in that period; or (ii) the debtor has become long-term insolvent because the value of its property is less than the sum of its obligations (over-indebtedness), or because the loss of the debtor capital company together with the loss brought forward in the current year exceeds half of the share capital, and the losses cannot be covered by profit brought forward or from reserves.
ES	The law lays down certain subjective and objective prerequisites to be met in order to open insolvency proceedings: (i) Subjective prerequisite: any debtor can be declared insolvent, whether a natural or legal person, an entrepreneur or a consumer, (ii) Objective prerequisite: the debtor's insolvency, defined as the inability to pay its liabilities on a regular basis.
SE	Insolvency is defined as a situation where the debtor is not able to duly pay his debts, and this inability is not of a temporary nature.

Source: Deloitte/Grimaldi (2022).

3.2 Special insolvency regime for micro- and small enterprises

Micro- and small enterprises (MSEs) rarely use formal insolvency proceedings voluntarily, and when they do it, it is almost inevitably too late to preserve their value. For micro and small companies (MSEs), the costs of proceedings can easily exceed the value of the estate. This is part of the reason why MSEs are often not wound down properly but remain in limbo. There is extensive evidence that traditional national insolvency frameworks are of no (or little) use for micro- and small enterprises. Traditional insolvency proceedings are too costly for such debtors, compared to the assets at hand belonging to the insolvency estate, or often simply not accessible to them (due to the lack of assets covering such costs).

Indeed, traditionally, special treatment for the so-called "small and medium-sized enterprises" has always been highly recommended, for instance, providing for a simplified application of restructuring or insolvency proceedings. Indeed, beyond such response by legislators, legal practice has underlined the need for the enterprises that do not meet certain thresholds to establish a preferred channel, due to their sizes.

A closer look at our analysis reveals that existing national regulations limit such privileges to businesses that do not exceed certain thresholds. While these thresholds are different across jurisdictions, the overall picture reveals that a special treatment is commonly only available for small, but not for medium sized businesses. Indeed, for medium sized businesses common insolvency and restructuring rules and procedures appear designed and applicable (although with some differences in the different member State).

These MSEs rarely use formal insolvency proceedings voluntarily, and when they do it, it is almost inevitably too late to preserve their value. This is, because:

(i) in the vast majority of cases, micro and small debtors have very little knowledge of their legal position, seek legal advice too late;

(ii) financial information available to SMEs is often poor, which hinders early awareness of the financial distress, but also

(iii) affects the ability of creditors to monitor the debtor;

(iv) most small businesses are family-run and constitute the family's only source of income, and the reputational stigma associated with formal insolvency proceedings remains significant.[310]

The main motivation of a dedicated MSE insolvency regime would be to reduce the costs of the procedure as reaction to the observation that traditional insolvency procedures are heavy and lead to legal costs that many defaulting MSEs are not able to cover.[311] Many MSEs are managed by entrepreneurs, which may cause a higher risk of opportunistic

[310] "Best practices in European restructuring", edited by L. Stanghellini, R. Mokal, C. Paulus, I. Tirado, 2018, p 233 et seq. This Final Report of the project "Contractualised distress resolution in the shadow of the law" was funded from the European Commission Grant JUST/2014/JCOO/AG/CIVI/7627.

[311] See Guerra-Martinez (2021) for an analysis of the specific issues of MSE insolvency regimes discussed in this paragraph.

behaviour than if the company is managed by an employed manager. The entrepreneur's emotional attachment to the company may furthermore generate a behavioural bias towards keeping even a non-viable company alive as long as possible, which reduces the recovery value. It also blocks production factors from a more productive use in other companies.

Creditors of MSEs may also be small and uninformed, implying that legal advice could be relatively costly for both creditors and debtors. Foreign investors may be less exposed to MSEs given their lower transaction value compared to larger companies. There may however be cases, especially in very innovative companies that are prepared to pay high risk premia where foreign creditors find interest. Given the general public interest in MSEs, there is a broader interest in making insolvency regimes also useful for MSEs. Since the bankruptcy of a MSE has direct consequences for the entrepreneur, interdependency with rules on second chance or debt discharge is a general concern.

The circumstance that domestic insolvency frameworks are not adapted properly to treat insolvent micro- and small enterprises represents a lost opportunity for the economy, by depriving those businesses from an orderly exit (if unviable) or from a sensible restructuring (if viable), and due to the sheer size of the community of such enterprises – to the internal market.

A simplification of rules as regards MSEs means a set of derogations from ordinary rules where such rules are considered overly cumbersome for the purposes of MSEs, rather than of a new separate procedure. Deviations from the general rules may include, for example, access to orderly proceedings regardless of assets available to cover the costs; easy entry conditions; lowered complexity and duration of the procedures; postponement of the payment of procedural costs; the possible public funding of procedural costs; rational creditors' passivity be considered as approval to decisions; administration of procedures mainly out-of-court; use of mandatory templates and of IT tools[312]; providing for a very short periods of a stay of a plan proposal.

More flexibility often means less safeguards for vulnerable stakeholders, which includes tort (i.e. involuntary) creditors and cross-border creditors (not likely to be numerous with these enterprises, though). It needs to be noted that the 2019 Restructuring Directive already provides for debt discharge for entrepreneurs. The overall trend, set by the World Bank, UNCITRAL or the United States is to simplify insolvency proceedings for MSEs[313].

[312] UNCITRAL recently adopted legislative recommendations for this purpose (as part 5 of its legislative guide).

[313] European Law Institute 2017 Instrument on insolvency law includes a specific chapter dedicated to this topic and relevant recommendations in this sense. US adopted federal legislation in 2019 – Small Business Reorganization Act (SBRA) which modified Chapter 11 of the Bankruptcy Code and which introduces a simplified sub-procedure to the famous Chapter 11 of the US Bankruptcy Code for small and medium enterprises. (first feedback from practice is positive).

Table A5.7: Existence of special rules for SMEs in EU Member States

AT	Not existent.
BE	In Belgium, in the framework of the transposition of the EU Directive 2019/1023, the Federal Parliament commissioned a group of experts to submit a transposition text for legislative approval. In the framework of the discussions in this expert group, the question of the treatment of SMEs is central and is being debated. Initially, it was planned to not apply the exemption for SMEs in Article 9(4)(3) of Directive 2019/1023, but recent discussions have brought this issue back into the spotlight.
BG	Not existent
HR	Currently, Croatian legislative framework does not provide for a specific treatment of SMEs. Special treatment has been reserved at this stage only for the companies of systemic importance for Republic of Croatia under the Law on the procedure of extraordinary administration in commercial companies of systemic importance for Republic of Croatia141. Companies of systemic importance are defined as joint stock companies (dionička društva), excluding credit and financial institutions, who cumulatively meet the following criteria: average of more than 5,000 employees in a calendar year, including its affiliated companies, and debt of more than HRK 7,500,000,000 (approx. EUR 1 billion), including its affiliated companies.
CY	There is no specific treatment of SMEs in insolvency regimes, except in the coordinated repayment plan, which is only available to company's employing less than 10 persons (this is the only requirement).
CZ	There are no special treatments for SMEs.
DK	Not existent
EE	No special rules for SMEs.
FI	There are no provisions on specific treatment of small and medium-sized enterprises (SMEs) within the Finnish insolvency regimes and the provisions on restructuring and bankruptcy proceedings are applicable to all Finnish entities regardless of their size.
FR	No information regarding a special insolvency procedure for SMEs. There is a simplified form of liquidation proceedings available for SMEs, which last for a maximum of 6 or 12 months, depending on the size.
DE	If the debtor is a small enterprise and does not have the financial means to hire a practitioner in the field of restructuring, there is the possibility of a 'light' version of restructuring proceedings (that is, a restructuring moderator (Sanierungsmoderator), who will negotiate the restructuring settlement agreement with the relevant creditors). This will require the confirmation by the rest ructuring court, but unlike the restructuring plan itself, it cannot be forced upon dissenting creditors.
EL	The new Bankruptcy Code provides for important amendments to the liquidation of small companies. The law identifies small and medium-sized entities as those that meet at least two of the following criteria: assets or property up to EUR 350 000 (from EUR150 000 that was until now), have a turnover amounting up to EUR 700 000 (from EUR 200 000 until now), and employ up to 10 people on average (from 5 persons until now). In case of individuals the asset criterion applies to the property of each individual ('small-scale bankruptcies'). The application for the declaration of small-scale bankruptcies is submitted electronically to the Electronic Solvency Register. Thirty days after the publication of the application in the Registry and unless an intervention against the application is submitted, the application is accepted by the Bankruptcy Court. The rapporteur and liquidator are appointed as well. The debtor loses the right to enjoy the benefits of a hearing, where he can present his arguments in a timely manner. Announcement of the creditors' claims must take place within three months of publication of the court's decision. Based on estimates by Institute of Small Companies-GSEBEE, 81% of small and medium-sized enterprises are potentially included in the new fast track bankruptcy regime, based on turnover (data from FHW GSEBEE climate survey July 2020).
HU	Insolvency regulations in Hungary are not different for large or small or medium-sized enterprises. The distinction is not justified either, as each enterprise operates according to the same principles and their organization is subject to similar rules.
IE	Not existent
IT	There is a derogatory regime - an 'early warning' procedure, aimed at detecting deterioration in a business at an early stage and thereby signalling to the debtor the need to act as a matter of urgency in order to: avoid insolvency; and continue its business activities.

	In general terms, the early warning procedure is an out-of-court procedure characterised by privacy and confidentiality. However, SMEs can apply to the court to obtain certain protective measures such as a stay from enforcement actions by the SMEs' creditors for a period of up to six months. The agreement entered into at the end of the early warning procedure has the same effect as a recovery plan underlying a voluntary composition agreement, thus exempting restructuring related transactions from insolvency avoidance actions
LV	There are no special rules for SMEs in Latvia.
LT	There are no specific rules concerning the insolvency of SMEs.
LU	Not found
MT	The liquidation proceedings in Malta are all designed for Small and Medium Enterprises (SMEs) because in Malta, over 95% of the companies are considered as SMEs
NL	Not existent.
PL	The current Polish Restructuring Law and the Bankruptcy law do not provide for a special treatment of micro and SMEs.
PT	SMEs are the focus of the Special Recovery Proceedings (Processo Especial de Revitalização – PER), which is found in CIRE. It was through this logic of 'preventive restructuring' that the PER was created to try to 'save' SMEs. In relation to SMEs, about insolvency proceedings, in addition to CIRE, the Extrajudicial Business Recovery Regime (RERE), and the Business Recovery Ombudsman (MRE) should be considered. The RERE is an instrument through which a debtor (except for natural persons who are not business owners) in a difficult economic situation or of eminent insolvency may enter into negotiations with all or some of its creditors with a view to reaching an agreement - voluntary, free-content and, as a rule, confidential - tending to its recovery. During a transitional period of 18 months from the date of its entry into force, debtors who are in a situation of insolvency, assessed under the terms of the CIRE, may resort to the RERE.
RO	Currently, there are no special tools or procedures used to help SMEs.
SK	No provisions found.
SI	Special rules for compulsory settlement proceedings over small, medium or large-sized company, imposed in section 4.8 of the Financial Operations, Insolvency Proceedings and Compulsory Winding-up Act (ZFPPIPP) regulate the following matters: the process of appointing insolvency practitioners in compulsory settlement proceedings, the creditor's proposal to initiate compulsory settlement proceedings, financial restructuring measures, lodging and testing of claims and value of collateral, re-compulsory settlement proceedings after final confirmation of compulsory settlement proceedings, creditors' agent.
ES	There are no specific rules for SMEs
SE	No specific rules for SMEs.

Source: Deloitte/Grimaldi (2022).

4. Distributional elements of insolvency

4.1 Ranking of claims

The notion of ranking of claims determines which class of creditors gets paid first from the proceeds of a liquidation. It also impacts on any restructuring negotiation to avoid insolvency, since it is the background against which creditors assess their options.

Regarding the issue of ranking of claims, insolvency law's core principle is that the distribution of the remaining value follows a system of priority established by law and separating between different classes of creditors whereby one can only proceed to payments on the claims of a lower class if the claims of the higher class have been fully satisfied. The treatment of secured creditors in insolvency is often also discussed as a matter of ranking. Their position is determined by national property law. The regime of how assets can be given as collateral with legal certainty is an important feature for businesses to obtain financing in an economy. This feature is thus one of the most

relevant elements in the creditors' ranking in the CMU context. Bank loans are usually secured (with collateral).

The issue of ranking claims can be resolved in as many ways as there are purposes of insolvency law. A simple comparison highlights this interrelationship: In France, the purpose of insolvency law is, among other things, but above all, to save as many jobs as possible, whereas in Germany the equivalent purpose.

The ranking of claims increases uncertainty for investors as they cannot know how much of the residual value of the company can be distributed among those creditors that do not enjoy preferential treatment. When a company is wound down, employees, tax authorities and other public authorities including those administering the procedure often enjoy preferential treatment that puts them on top of other creditors.

The ranking of claims tends to be complex, which make the outcome very difficult to anticipate for foreign investors since they may have neither a good understanding of the rules in the destination country, how they area applied and how large the share of these preferential creditors could be. They have therefore little possibility to assess the impact of creditor ranking on the recovery value and the recovery time.

The rules on ranking of claims, and in particular those related to the protection of secured credits, are of particular importance for foreign investors when they try to anticipate the risks attached to their investments, as these affect the expected recovery rates. Divergences in this area may thus have a significant impact on the cost of lending to reflect such risks, and – in certain cases – may serve as a deterrent from engagement for investors.

The principle of pari passu (alternatively: *par condicio creditorum*) constitutes a fundamental principle of equity which implies that in a common situation (such as an insolvency procedure) where the debtor's existing assets are insufficient to satisfy all his creditors in full, losses are shared proportionally and equitably. However, this principle has rarely - if ever - been applied without friction. The history of insolvency law can be written in terms of an ongoing struggle for privileged status, i.e., a higher rank.

In many Member States, vulnerable creditor groups such as employees rank first. In other Member States, employees' rights are protected by social security systems, including e.g. funds to pay outstanding wages. Outstanding taxes make up the bulk of the claims in many insolvency proceedings, in particular for SMEs, and in some Member States, they rank first (aka the fiscal privilege). They also stand in the way of many restructurings because the administration does not have discretion to forgive tax debts.

More specifically insolvency regimes respect security rights arrangements of the debtor as long as they are permitted under local civil/contract law and do not constitute a fraudulent transfer of assets under respective insolvency law provisions. Indeed, secured transactions play a key role in a well-functioning market economy and discrepancies and

uncertainties in the legal framework governing security rights are the main reasons for the high costs and unavailability of credit[314].

Post-commencement preferences are justified on the basis of a specific legitimate interest defined in advance to allow each creditor to calculate ex ante their risks in view of the legal position in a possible future insolvency of their debtor. Thus, to ensure a proper functioning of the market, having regards to the creditors' perspective, what matters is to identify which are the legitimate interests which justify these preferences interference with the pre-commencement entitlements. It is obvious that these legitimate interests have to be identified in the interests of all the creditors in so far they provide a priority over the ordinary claims (i.e., so called super -priority).

The first legitimate interest is to guarantee orderly procedures by securing the payment of costs of proceedings. The proper and correct functioning of the systems ultimate safeguards the interests and rights of all the stakeholders. Administrative expenses (i.e., claims resulting from the debtors' estate) should be granted with a priority as well considering that they are costs resulting from the efforts to organise and orderly liquidate all assets in the estate or reorganise the debtor's business in the interest of all creditors. The second legitimate interest is in securing the going concern (in a going concern sale as well as in a piecemeal auction process, i.e., prepack sale) which is possible only of if the assets forming the business are not torn apart at the outset of proceedings by secured creditors who enforces their pre-commencement entitlements. In effect, a going concern sale or a prepack sale usually means a higher return for creditors than the receivables from a piecemeal liquidation.

Lastly, a further legitimate interest may be identified in the protection of interim and/or new financing as far as it sustains the restructuring proceedings or the sales as a going concern (see para below on treatment of interim or new financing). As of today, claims from interim finance enjoy the priority of administrative expenses, which means they usually rank ahead of pre-commencement creditors, but not affect the rights of secured creditors. In Belgium, however, interim finance may rank ahead of secured creditors. when and to the extent that secured creditors have benefited from such finance themselves. In France, for example, a super-priority is reported meaning that claims deriving from new finance arrangements in a safeguard proceeding or a judicial reorganization even rank above other secured and unsecured creditors. In Italy, in arrangement with creditors and in debt restructuring agreements, both interim and new finance – consequential to these agreements – are ranked ahead of secured creditors.

Where securing the claim induces creditors to invest more funds, ultimately encouraging the credit system, providing super-priorities not grounded in the interests of all creditors makes it extremely difficult to ex ante assess the extent of super-preferred claims and, thus, almost impossible to precisely calculate credit risks which usually makes credit more expensive.

Table A5.8 Rules and practices in EU Member States on the ranking of creditors

	Types of creditors	**Ranking**

[314] World Bank, Principles for Effective Insolvency and Creditor/Debtor Regimes, cit. See principles A2; A3.

AT	secured (or preferential), and unsecured creditors.	Priority claims are defined as claims against the insolvency estate that are satisfied prior to all other insolvency creditors. Priority claims are reduced to certain kinds of claims and include: • costs of the proceedings, • costs regarding administration, sustainment and supply of the insolvency estate, • claims of the employees for current salary, • claims in connection with the termination of certain kinds of employees, claims resulting from the fulfilment of certain contracts, • claims based on transactions processed by the insolvency administrator, • claims based on unjust enrichment of the insolvency estate, and • compensation for the members of privileged associations for the protection of creditors' rights. Filing priority claims with the insolvency court separately is not required. These claims are filed directly with the insolvency administrator.
BE	Under Art. 2 of BCEL, the following categories of creditors can be distinguished, each subsequent category holding a lower priority against the previous one: • Preferential creditors: ✓ Special privilege, ✓ General privilege, • ordinary creditors.	The competing claims to the estate in bankruptcy occur automatically under law. The bankrupt debtor's assets are used exclusively to satisfy creditors existing on the day of bankruptcy and whose claim is fixed on the day of bankruptcy. In principle, an equal distribution among the creditors will take place, except when the regime of mortgages and liens allows for derogations. When a bankrupt's property is realised, liens and mortgages entitle the lien holder to be paid preferentially from the proceeds with priority over other unsecured creditors. The '*debts of the bankruptcy estate'* (management costs and expenses, taxes, environmental debts, debts arising from the trustee in bankruptcy's initiatives or quasi-contracts) constitute preferential claims on the estate in bankruptcy.
BG	Creditors are divided into several classes according to Art. 722 of the BCA, each subsequent class having a lower priority against the previous one: • Secured creditors (mortgage, property subject to lien etc.); • Privileged creditors: employment, bankruptcy costs etc.; • Unsecured creditors.	The following procedure for settling claims by way of making distributions from the estate converted into money, stipulated in Article 722 of the Commerce Act, is followed: • claims secured by a pledge or mortgage, garnishment or distraint, registered in accordance with the Liens Act — from the proceeds from security realisation; • claims in respect of which the right to lien is exercised — from the value of the asset subject to lien; • expenses incurred in the insolvency proceedings (stamp duty payable upon filing and all other expenses incurred until the entry into force of the ruling opening insolvency proceedings; the receiver's remuneration; the claims of workers and employees when the debtor's enterprise has not ceased trading; the costs incurred on augmentation, administration, valuation and distribution of the insolvency estate; and the maintenance payments in favour of the debtor and their family); • claims arising from employment contracts that existed before insolvency proceedings were opened; • statutory compensation payable to third parties by the debtor; • public-law debts to the central government or municipalities, including but not limited to those arising from taxes, customs duties, fees and mandatory social security contributions, if they arose before the date on which insolvency proceedings were opened; • claims that arose after the commencement of insolvency and unpaid by the respective due date; • any remaining unsecured claims that arose before insolvency proceedings were opened; • statutory or contractual interest on unsecured debts due after the date on which insolvency proceedings were opened; • loans granted to the debtor by a business partner or shareholder; • donations; • the expenses incurred by the creditors in connection with the insolvency proceedings, except for the expenses under Article 629b of the Commerce Act (prepaid initial litigation expenses).
HR	As a general rule,	Pursuant to the CBL, claims and their creditors are ranked respectively as it

	bankruptcy creditors are classified in payment ranks according to their claims. Creditors of subsequent payment rank cannot be settled until the creditors from the previous rank have been completely settled. Creditors of the same payment rank will be settled proportionally to their claims.	follows: • bankruptcy estate – claims of the bankruptcy estate include bankruptcy proceedings costs and other claims of the bankruptcy estate (attorney claims etc.); • creditors with separate satisfactory right– are not bankruptcy creditors and they may request extraction of objects to which they are entitled out of the bankruptcy estate; • secured creditors– their claims are satisfied from secured assets. Secured creditors are also bankruptcy creditors only if the debtor is personally liable to them, and they are entitled to satisfy their claims from the bankruptcy estate only if they waived their right of satisfaction from the secured assets or are unable to do so; • regular bankruptcy creditors– are unsubordinated and unsecured creditors whose claims are classified into ranks depending on the particular claim as follows: first rank – claims of employees and of former employees of the bankruptcy debtor which arose from employment until the opening of the bankruptcy proceedings and certain related claims, second rank – all the other claims towards the bankruptcy debtor, except for the subordinated claims, • subordinated bankruptcy creditors– are the last in line for settlement and their rank within the group depends on the type of their claim.
CY	In Cyprus, creditors are divided in: • secured creditors; • preferential creditors, and; • unsecured creditors.	The order of distribution of assets in all forms of winding-up and in receivership is as follows: • the costs of the winding-up; • the preferential debts. Preferential claims are defined in section 300 of the Companies Law and comprise: all government and local taxes and duties due at the date of liquidation and having become due and payable within 12 months before that date and, in the case of assessed taxes, not exceeding one year's assessment; all sums due to employees, including wages, up to one year's accrued holiday pay, deductions from wages (such as provident fund contributions) and compensation for injury. Claims of employees who are shareholders or directors may not rank as preferential depending on the nature of the shareholding or directorship (*section 300(1), Companies Law, Cap. 113*). A person who has advanced funds to pay employees will have a subrogated preferential claim to the extent that the employees' direct preferential claims have been diminished because of the advances (*Sec 300(2), CCL*). • any amount secured by a floating charge; • the unsecured ordinary creditors; • any deferred debts such as sums due to members in respect of dividends declared but not paid; • any share capital of the company. Where there are different classes of share capital, such as preference shares, their respective rankings will be determined by the terms on which they were issued.
CZ	There are three categories of creditors: • secured creditors; • preferential creditors; e.g. insolvency administrator, state authorities, employees, suppliers delivering their supply after decision on insolvency; • unsecured creditors.	After the decision approving the final report becomes final, the insolvency practitioner submits a draft order on the distribution of the estate to the insolvency court, stating how much should be paid for each claim in the revised list of registered claims. On that basis, the insolvency court issues an order on the distribution of the estate, in which it determines the amounts to be paid to creditors. All creditors included in the distribution schedule are satisfied in proportion to the ascertained amount of their claim. Before the distribution, as yet unpaid claims which may be met at any time during the bankruptcy proceedings are met, specifically: • claims against the estate – the cash expenses and fee of the insolvency practitioner, costs associated with the maintenance and administration of the debtor's estate, taxes, charges, social security contributions, the state employment policy contribution, public health insurance contributions, etc.;

		• equivalent claims – the labour-law claims of the debtor's employees, creditors' claims to compensation for damage to health, government claims, etc.; • secured claims.
DK	Danish insolvency law does not divide creditors into classes, apart from (fully) secured and unsecured creditors. Creditors with valid and enforceable security do not form part of the ranking. However, if the security does not fully cover a creditor's claim, they are viewed as an unsecured creditor in relation to the unsecured part of their claim.	The order of priority of the creditors is governed by the DBA. The order is the following: • Costs and fees related to the administration of the estate; • Costs related to a vain restructuring attempt or vain attempts at an overall arrangement with the debtor's creditors prior to the bankruptcy; • Employees' claims; • Duties on goods that are subject to duty, e.g. alcoholic and tobacco goods; • Unsecured creditors, e.g. an ordinary receivable based on an invoice, tax and VAT claims etc.; • Claims for interest after the issue of the bankruptcy order, gifts and fines.
EE	The creditors are divided into: • secured creditors; • unsecured creditors.	Before money is paid on the basis of distribution ratios, payments relating to bankruptcy proceedings are made out of the bankruptcy estate in the following order: • claims arising from the consequences of exclusion or recovery of assets; • maintenance support payable to the debtor and their dependants; • consolidated obligations; • costs and expenses incurred in the bankruptcy proceedings. After these payments have been made, the creditors' claims are satisfied in the following order: • admitted claims secured by a pledge; • other admitted claims that were lodged within the term set; • other claims that were not lodged within the term set, but that were admitted.
FI	The three typical creditor classes are secured creditors, unsecured creditors and floating charge holders.	According to Ranking Act, the priority order of creditors is, as follows: • Secured creditors to the extent of the value of the secured asset; • Preferential claims: court fees, the bankruptcy trustee's fees, debt incurred during the proceedings, i.e. after the court's decision; • Priority claims: creditors holding a business mortgage; • The claims that are satisfied last according to the Act on the Ranking of Claims are: • interest and penalty for late payment for the period after the commencement of the bankruptcy; • certain public penalties imposed on the debtor as a result of a criminal offense or illegal proceedings; • a claim based on a bond issued by the debtor company if the terms of the loan provide a lower priority than the other obligations of the issuer; • a claim based on a loan that may be paid with its interest in the event of bankruptcy only with a lower priority to all other creditors; and • a claim based on the Gift Promises Act (625/1947, as amended).
FR	Creditors are divided into: • preferential creditors (both secured and preferential rights), or; • unsecured creditors. A creditor may thus have preferential status: • because he is in possession of a guarantee granted by his debtor or obtained	Preferential creditors are not all equal. Where several preferential creditors compete, they are paid in an order fixed by law, but still before the unsecured creditors. The unsecured creditors are paid from the debtor's remaining assets, after payment of the preferential creditors. The distribution is carried out on a pro rata basis. The following ranking is applicable: • 'Super preference' of wage claims: payment of remuneration for the last 60 days of work prior to the judgment opening the proceedings; • Court costs duly arising after the judgment opening the proceedings to meet the requirements of conducting the proceedings: costs relating to preservation, realisation of assets and distribution of proceeds among the creditors (inventory and advertising costs, remuneration of court-

	from a court decision, or • because a preferential right is conferred on him by law due to his status.	appointed representatives, etc.); • Claims guaranteed by the conciliation preference: benefits creditors who provide a fresh injection of cash or supply new goods or services with a view to ensuring the continuation and survival of the business; • Preference of claims arising after the judgment opening the proceedings: claims arising to meet the requirements of conducting the proceedings or of provisional maintenance of the business, or claims arising in exchange for goods or services supplied to the debtor during the maintenance of the business or to perform a current contract maintained by the liquidator, or claims arising for the everyday needs of the debtor who is a natural person; • Claims guaranteed by the general preference of employees: payment of the remuneration for six months of work prior to the judgment opening the proceedings; • Claims guaranteed by a special preference or by a mortgage; • Unsecured claims.

DE	Creditors are divided into:
	• secured creditors;
	• unsecured creditors; and
	• subordinated creditors.
		In regular insolvency proceedings (*Regelinsolvenz)* as well as in procedures with an insolvency plan (*Insolvenzplan)*, creditors and contributories rank as follows on a debtor's insolvency:
		• Owners. Any assets, which belong to third parties, must be surrendered to these owners;
		• Secured creditors (immovable property). A land charge or mortgage holder has a claim for foreclosure;
		• Secured creditors (movable assets, and claims). Secured debts are paid using the sale proceeds of the relevant assets. An insolvency administrator is generally entitled to sell such encumbered assets to a third party free from encumbrances, or to collect such encumbered claims. The insolvency administrator disburses the proceeds to the secured creditor up to a maximum amount of the secured claim, and he/she will withhold a standard fee of 9% from the respective proceeds for the insolvency estate. Any surplus in excess of the secured claim will remain with the insolvency estate and will become available to other creditors;
		• Expenses/costs of insolvency proceedings. This includes court fees for the insolvency proceedings, remuneration earned and expenses incurred by the preliminary insolvency administrator, the insolvency administrator and the members of the creditors' committee. The expenses/costs of insolvency proceedings rank in higher priority to all other debts (including employees);
		• Insolvency estate creditors. These are claims entitled to full satisfaction and include, for example, claims resulting from new contracts entered into by the insolvency administrator with third parties, such as suppliers;
		• Insolvency creditors. All unsecured creditors (including employees) who registered their claims in writing with the insolvency administrator and whose claims have seen no objection by the insolvency administrator or an insolvency creditor. Insolvency creditors will receive payment on a pro rata basis;
		• Subordinated creditors. Subordinated claims are (among others):
		  • claims for payment of interest accrued after the opening of insolvency proceedings;
		  • costs incurred by individual insolvency creditors due to their participation in the insolvency proceedings;
		  • claims for repayment of shareholder loans or similar claims.
		• Claims subordinated by agreement. Such claims rank behind statutory subordinated claims;
		• Shareholders. Any remaining surplus will be distributed to the debtor, or in the case of companies, to the shareholders.

EL	Articles 975–978 of the Code of Civil Procedure include specific provisions on the priority of claims of	The distinction between claims with a general privilege, claims with a special privilege and unsecured claims is critical in the context of distribution of the proceeds of liquidation of the assets over which security has been created. Claims with a general or special privilege are satisfied in priority over unsecured claims.

	creditors and distinguish between: • claims with a general privilege, which applies by operation of law and concerns, among others, claims on account of valued added tax and other taxes, claims of public law entities, claims of employees and social security funds; • claims with a special privilege, which include those of secured creditors; and • unsecured claims.	Under Article 977 of the Greek Code of Civil Procedure, if there are only claims with a general privilege and claims with a special privilege, the former may only be satisfied up to one-third of the proceeds of liquidation of the bankruptcy estate. If there are claims of all three categories, those with a general privilege are satisfied up to 25 per cent, those with a special privilege are satisfied up to 65 per cent and unsecured claims are satisfied up to 10 per cent of the proceeds of liquidation of the bankruptcy estate. If there are no claims with a special privilege, those with a general privilege are satisfied up to 70 per cent and unsecured claims are satisfied up to 30 per cent of the proceeds of liquidation of the bankruptcy estate. If there are only claims with a special privilege and unsecured claims, those with a special privilege are satisfied up to 90 per cent and unsecured claims are satisfied up to 10 per cent of the proceeds of liquidation of the bankruptcy estate.
HU	Creditors are divided into: • secured creditors; • unsecured creditors.	The order of payment of creditors is as follows: • the costs of liquidation; • the unsatisfied part of the pledged receivables (secured claim) incurred before the commencement date of the liquidation up to the amount of the sales revenue of the pledged property excluding VAT, so that the amount deducted at the time of payment to the pledgee and the amount set aside for debts shall be used to pay the pledged receivables; • alimony, life annuity, compensation annuity, mining supplement, and cash benefits paid to a member of an agricultural cooperative in lieu of backyard land or crops, which are due to the holder for the rest of his life; • other claims of private persons arising from a non-economic activity, other than claims based on a bond (including, in particular, claims arising from defective performance, damages, including the amount quantified by the liquidator in the ordinary course of business-related warranty or guarantee obligations), the claims of small and micro enterprises, primary agricultural producers and the claims of the Common Fund of Cooperative Credit Institutions based on the fact that the Common Fund of Cooperative Credit Institution has become the legal successor of the depositors with the insured deposit or the holder of their claims; • overdue social security contributions and private pension fund membership fees, taxes and public debts collectable as taxes, as well as grants from other international sources based on repayable public finances, the European Union or an international agreement, as well as utilities and condominium costs and claims on the Cooperative Credit Institutions' Common Fund for Equity, other than those referred to in point (d); • claims of other unsecured creditors; • default interest and default penalties irrespectively of the date and legal ground of their arising, as well as debts of a surcharge and fine; and • claims owed to directors, executive position employees of the debtor or by their spouses or close relatives, or claims of companies under the influence of the debtor, claims originating from agreements without consideration and claims owed to a member (shareholder) having a majority influence in the debtor (excluding mandatory minimum wage, wage and salary claims not exceeding twice the guaranteed wage and not exceeding six months' average wage in the case of an employee paid exclusively for performance pay).
IE	Creditors are divided into: • preferential creditors;	Preferential Debt: In Personal Insolvency Arrangements (PIA) and Debt Settlement Arrangements (DSA), preferential debts are paid per the terms of the agreement, and in bankruptcy preferential debts rank directly after bankruptcy fees and any costs or expenses incurred by the Official

	• secured creditors; • unsecured creditors	Assignee (OA) when dealing with the bankruptcy estate. Debts that are considered to be preferential are: • Certain amounts due to the Revenue Commissioners, such as Income Tax, Capital Gains Tax, VAT, PAYE/PRSI etc.; • Certain Local Authority Rates incurred in the 12 months prior to the debtor's date of adjudication or entering into the arrangement (commencement date). This includes local council rates and charges; • Wages or salaries owed to any employees of the debtor for the 4 months previous to the commencement date; • Any pension-related, holiday-related or sick absence pay due to these employees. Secured Debt: In a PIA, the secured creditor is bound by the terms of the agreement. In a normal PIA the secured lender is paid out of the debtor's income at whatever figure is agreed to in the arrangement. The debtor's remaining monthly income, if any, after the debtor's RLEs and PIP's fees are deducted is paid to their unsecured creditors by way of dividend. Bankruptcy does not affect the rights of a secured creditor. Such a creditor may take one of the following three options with regard their secured debt: • Rely on their security – this means they effectively stay outside the bankruptcy; • Realise or value their security and claim for the shortfall (if any) – the creditor will calculate the fair market value of the secured asset and subtract this from the total owing. The resultant shortfall (if any) is admitted into the bankruptcy estate as an unsecured claim. During this process, the secured creditor may sell the asset in question; • Abandon their security – the secured creditor has an option to abandon their security entirely and have their claim admitted into the bankruptcy estate as an unsecured claim. Unsecured Debt: In both a PIA and a DSA, the debts of unsecured creditors are settled under the agreed terms of the arrangement. In a DRN if a person's circumstances improve during the supervision period, s/he must tell the ISI and depending on the level of change, may be asked to make some contribution to what he/she owes. The claims of unsecured creditors of a bankruptcy estate are ranked equally. Their debts are settled with the disbursement of any funds that remain after bankruptcy fees, OA expenses and preferential debts have been settled.
IT	Creditors are divided into: • secured creditors and • unsecured creditors. There are three categories of claims: • senior-ranked claims; • secured claims, i.e. claims with priority; • unsecured, i.e. unsecured claims.	Article 111 of the IBL lays down preference criteria for the method of liquidation of these claims. According to that article, the sums obtained from the liquidation must be disbursed in the following order: • to mortgage and pledge claims, in order to the liquidation of the secured assets; • senior-ranked claims; • other creditors who have a right of pre-emption; • unsecured creditors. Senior-ranked claims must be satisfied in their entirety, provided that the assets are sufficient, but even for these there may be causes of pre-emption, which must be taken into account in their liquidation. Such claims are those so defined by law (*e.g.* in the case of the provisional exercise of the business by the bankrupt). If the assets are insufficient, senior-ranked claims must be distributed according to the criteria of graduation and proportionality, in accordance with the order assigned by the law (Article 111-bis, IBL). Article 111- bis makes an exception to this principle, stating that '*the proceeds from the liquidation of assets subject to pledge and mortgage for the part intended for secured creditors' cannot be allocated to satisfy senior-ranked claims*.' As regards preferential creditors, which may be either creditors with a general or special lien (Article 2745 et seq. of the Civil Code) or creditors secured by a pledge or mortgage, the reference article is 111-quater of the Bankruptcy Law and Articles 54 and 55 of the Bankruptcy Law. In particular, claims secured by a general lien have a right of pre-emption for the capital, expenses and interest, within the limits set out in Articles 54

		and 55, on the price obtained from the liquidation of the movable assets, on which they compete in a single ranking with claims secured by a special lien on movable assets, according to the degree provided for by law. Claims secured by mortgage and lien and those secured by special privilege shall have a right of pre-emption for the principal, expenses and interest, within the limits set out in Articles 54 and 55, on the price obtained from the assets pledged as collateral. If the security has not yet been realized, or for the part for which they remain unsatisfied by the security, they shall participate in the distribution of the assets in the same manner and in competition with the unsecured, that is to say in proportion to the amount of the claim for which they have been admitted.
LV	Information not available.	
LT	Bankruptcies, creditors' claims are satisfied in two stages. At the first stage, creditors' claims are paid without the interest and default penalties; interest and penalties are paid at the second stage. At each stage, the creditor's claims of each lower rank are satisfied after the creditor's claims of the superior rank in the respective stage have been completely satisfied. If the assets are insufficient to fully satisfy the claims of one rank in one stage, the said claims are to be satisfied in proportion to the amount due to each creditor. • First-rank claims are employee claims arising out of the employment relationship; claims for damage compensation due to mutilation or other bodily injury, contraction of an occupational disease or death as a result of an accident at work; and claims of agricultural businesses requesting payment for agricultural products sold; • Second-rank claims are claims in respect of taxes and other contributions to State and social insurance budgets and compulsory health insurance contributions; in respect of money borrowed on behalf of the State and loans secured by a guarantee provided by the State or a guarantee institution vouched for by the State; and in respect of support granted from European Union funds and State budget funds. All other claims from creditors are third-rank claims.	
LU	Some creditors with a security or preferential claim are paid first. Preferential creditors are ranked in a legal order that is public policy (property landlords, mortgagees, creditors with securities over the business capital and, in particular, the public treasury in the broadest sense). In general, the trustee refers to Articles 2096 to 2098, 2101 and 2102 of the Civil Code (*Code civil*). The net assets available to unsecured creditors must be distributed on a pro rata basis in accordance with Article 561(1) of the Commercial Code. Once the trustee knows the amount of the fees set by the court, has ranked the preferential creditors and knows the amount left to be distributed between the unsecured creditors, he/she draws up an asset distribution plan that is submitted in the first instance to the official receiver. In accordance with Article 533 of the Commercial Code, the trustee invites all creditors to the presentation of accounts meeting by registered letter, to which he/she attaches a copy of the asset distribution plan.	
MT	Under Maltese legislation there is no definite list of ranking of creditors, since ranking is not found in a specific legislation but is found in various legislation. The legislation which deals with ranking of claims can: be found in • Article 302 of Chapter 386 MCA states that in the winding up of a company the assets of which are insufficient to meet the liabilities, the rights of secured and unsecured creditors and the priority and ranking of their debts shall be regulated by the law for the time being in force; • Article 535 of Chapter 13 MCA also states that creditors having pledges, privileges or hypothecs shall be ranked according to the law for the time being in force. In both cases the law states that ranking of debt shall be regulated by the law for the time being in force. Various specific laws which grant priorities to certain claims, as is the case with the Value Added Tax Act, the Employment and Industrial Relations Act, and the Social Security Act.	
NL	A leading principle of Dutch bankruptcy law is the *paritas creditorum* (*pari passum*), which means that all creditors have an equal right to the debtor's assets and that the proceeds of the bankrupt estate are distributed among them *pro rata parte*. However, there are creditors to whom the principle of *paritas creditorum* (*pari passum*) does not apply: • Creditors that hold a security interest; and • Creditors that have a preference by virtue of law. Therefore, the *paritas creditorum (pari passum)* applies to those who have an unsecured claim and do not have a right of preference, *i.e.* the ordinary creditors share *pro rata parte* in the amount available to them. A further exception can be made for subordinated claims.	
PL	The claims to be paid out of the bankruptcy estate fall into the following categories: • the first category - claims under an employment relationship for the period before the declaration of bankruptcy (applies mutatis mutandis to the claims of the Fund for Guaranteed Employee Benefits for the repayment, out of the bankruptcy estate, of benefits paid out to the bankrupt party's employees) ;	

	• the second category - other claims, if not met in other categories, in particular taxes and public levies as well as other claims in respect of social insurance contributions; • the third category - interest on claims included in the categories above, in the order in which the principal amounts are paid as well as court and administrative fines and claims regarding donations and legacies; • the fourth category - partners' or shareholders' claims regarding a loan or another legal act with similar effects, especially the supply of goods on deferred terms to the bankrupt party that was a capital company in the five years preceding the declaration of bankruptcy, with interest. The sum falling to the creditor is counted first of all towards the main claim, then to interest and other collateral claims, with the costs of proceedings being covered at the end. Claims secured with a mortgage, pledge, registered pledge, fiscal pledge and maritime mortgage as well as rights expiring according to the provisions of the Act and the effects of disclosing personal rights and claims encumbering real property, a right to perpetual usufruct, a cooperative member's ownership right to residential premises or a sea-going vessel entered in the shipping register, are met out of the sum obtained through the liquidation of the encumbered party minus the costs of liquidating that party and other costs of bankruptcy proceedings in an amount no higher than a tenth of the sum obtained through the liquidation; however, the deducted part of the costs of bankruptcy proceedings cannot be higher than the part corresponding to the proportion of the value of the encumbered object to the value of the total bankruptcy estate. Those claims and rights are met in the order of their priority. If the sum obtained through the liquidation of the encumbered party is used to meet both claims secured by a mortgage and expiring rights as well as personal rights and claims, the priority depends on the moment as which the entry of a mortgage, right or claim in the land and mortgage register begins to have effect.
PT	The graduation of claims and corresponding hierarchy or priority of payment shall take place in the following order: • secured claims; • privileged claims • common claims; and • subordinated claims. <u>The secured claims:</u> Secured claims are the ones that benefit from real guarantees, including special credit privileges, up to the value of the assets subject to the guarantee, are paid. Secured credits are credits benefiting from: mortgage, pledge, special credit privileges, right of retention, among others. Secured credits are only paid with the proceeds of the sale of the assets encumbered by the guarantee, after: • deduction of the costs of the respective settlement (payment of any commissions to auctioneers, costs of notarial acts such as the execution of the public deed or the authentication instrument, etc.) and; • deducting 10% of the sale proceeds to pay the insolvent estate's debts. <u>Privileged claims:</u> In second place and, if the balance remains, the privileged credits are paid, which are the credits that benefit from general, movable or immovable privileges of credit. General preferential claims are those that apply to the generality of the debtor's assets. Only claims that benefit from general preferential claims are classified as preferential claims and not those that benefit from special preferential claims, which are those that are over specific assets of the debtor. In effect, special preferential claims are considered as real guarantees and are therefore classified as secured claims. <u>Common claims:</u> In the third place and if the balance subsists, the common claims are paid, which are the claims that do not benefit from real guarantees (secured claims), nor from general privileges of credit (privileged claims), nor do they qualify as subordinated claims. Thus, common claims are, for example: • credits that benefit only from personal guarantees, such as surety and personal guarantee; • credits that, despite benefiting from a real security, have not been able to be paid with the value of the sale of the secured asset, as mentioned above under the heading '1st place, secured credits'; • credits whose real security had been extinguished upon the declaration of insolvency (this is the case of some general and special privileges of the State, among others); • claims whose security in rem is completely removed in the context of insolvency proceedings. This is the case of claims secured by a real guarantee of a procedural nature, such as seizure, attachment and judicial mortgage. <u>Subordinated claims:</u> In 4th and last place, if a balance still remains (which is very unlikely), subordinated claims are paid. Subordinated claims are, for example: • claims held by persons especially related to the debtor, whether a natural or legal person; or the, • claims for shareholder loans held by the partners of private limited companies or single partner limited companies, among others.
RO	The funds obtained from the sale of assets and rights from the debtor's estate which are secured in favour

	of the creditor on a preferential basis will be distributed in the following order: • fees, stamp duties and any other expenditure arising out of the sale of the assets concerned, including expenses required for the conservation and administration of those assets, expenses incurred by the creditor under the forced recovery procedure, claims of utilities suppliers which arise after the opening of the procedure, and remuneration due to persons employed in the common interest of all creditors on the date of distribution, which will be borne on a pro rata basis in proportion to the value of all the debtor's assets; • claims of creditors enjoying preference that arise during the insolvency proceedings; these claims include capital, interest and other ancillaries, where applicable; • claims of creditors enjoying preference, including the entire capital, interest, and increases and penalties of any kind. If the sums realised from the sale of these assets is insufficient for the full payment of the claims concerned, the creditors have an unsecured or public budget claim, as the case may be, for the difference, which will be ranked with the other claims in the appropriate category. If, after the payment of the sums referred to previously, a surplus remains, it will be deposited by the court-appointed liquidator in the account of the debtor's estate..
SK	In bankruptcy proceedings, the distribution of the proceeds varies according to the type of creditor: • secured creditors, • unsecured creditors, • creditors with subordinated claims, • contractual penalties and claims from creditors related to the debtor. A creditor may lodge all claims against the debtor, including claims that are not yet due for payment. A secured claim (with a security interest in the debtor's assets) can also be lodged. A secured claim a creditor has against a person other than the debtor can be lodged if the security interest concerns the debtor's assets (there are certain restrictions on satisfaction in such cases); if such a claim is not lodged, it is treated as a weaker claim against the estate. Future claims and contingent claims can also be lodged. Claims that are not lodged by means of an application are called claims against the estate. They are divided into claims against the general estate and claims against a separate estate (secured with a security interest). The insolvency practitioner satisfies claims against the general estate on an ongoing basis; if claims of the same ranking against the general estate cannot be fully satisfied, they are satisfied proportionally. Claims against a separate estate relate to the separate estate. The insolvency practitioner satisfies claims against the separate estate on an ongoing basis; if claims of the same ranking against the separate estate cannot be fully satisfied, they are satisfied proportionally.
SI	The level of priority of creditors in insolvency proceedings is determined in ZFPPIPP (in descending order) is: • creditors with secured claims (creditors with a right to separate satisfaction) and exclusionary creditors (creditor with an exclusion right), • creditors with unsecured priority claims (salaries, compensations, taxes etc.), • creditors with unsecured ordinary claims and, creditors with unsecured subordinated claims.
ES	Once insolvency proceedings are opened, the claims of all of the creditors, whether unsecured or preferential are included among the debtor's liabilities. The purpose here, based on the principles of *parcondicio creditorum* (*pari passu*) and compliance with the '*dividend law'*, is to give all claims equal treatment in the context of the debtor's verified insolvency and when it comes to settling all of its debts. There is a difference in creditors and their respective claims: <u>Claims with special preference (Article 270) include:</u> • Claims secured with a real estate mortgage, a chattel mortgage, or with a registered lien on the mortgaged or pledged assets or rights; • Claims secured by the pledging of income from encumbered property; • Loan claims on fixed assets, including the claims of workers on the objects manufactured by them while they are the property or in the possession of the debtor; • Claims on financial lease payments or purchase at fixed prices of movable or immovable assets, to the benefit of the lessors or sellers and, if applicable, the financial backers, on assets leased or sold with reservation of title, with a prohibition on disposal or with a condition subsequent in the case of non-payment; • Claims guaranteed with securities represented in account entries, on the encumbered securities; • Claims secured by a pledge established in public documents, on pledged assets or rights that are in the possession of the creditor or of a third party. <u>Claims with general preference (Article 280) include:</u> • Wage claims; • The amounts corresponding to tax and social security withholdings owed by the debtor in compliance with a legal obligation;

	• Claims of natural persons arising from freelance work and those that correspond to authors for the assignment of the exploitation rights of works subject to intellectual property protection, accrued during the six months prior to the insolvency order; • Tax claims and other public law claims. This preferential right may be applied to up to 50 % of the overall claims of the tax authority and the overall claims of the social security system, respectively; • Claims for non-contractual civil liability; • Claims arising from new cash income granted in the context of a refinancing agreement that meets the conditions laid down in Article 71(6) and of the amount not recognised as a claim against the insolvency estate; • Up to 50 % of the amount of the claims held by the creditor that applied for the insolvency proceedings and which are not considered subordinate. Subordinate claims (Article 281) include: • Claims that have been communicated late, except where these relate to claims under forced recognition or due to court decisions; • Claims that, on the basis of contractual agreement, are subordinated; • Claims for surcharges and interest; • Claims for fines and penalties; • Claims held by any persons with a special relationship with the debtor under the terms established in this Law; • Claims arising from revocatory actions due to a person having been declared to have acted in bad faith in the contested act; • Claims arising from contracts with reciprocal obligations or, in the case of reinstatement, in the situations laid down in the provision.
SE	The Preference Act regulates the entitlements of the creditors to receive payment in the event of bankruptcy. Creditor with preference is either special or general. A special preference relates to certain property (examples being a right of pledge, a right of retention, or a mortgage on immovable property). A general preference relates to all property included in the debtor's bankruptcy estate. A special preference takes precedence over a general preference. Any claims that do not enjoy a preference have the same rights among themselves. It may also have been provided in an agreement that a creditor is entitled to payment only after all other creditors have been satisfied A preference continues in being even if the claim is transferred or attached or otherwise passes to another party. If a claim enjoys a special preference with respect to certain property, but the property in question is insufficient to satisfy the claim, the remainder is treated as a claim without preference.

Source: Deloitte/Grimaldi (2022)

4.2 Creditor committees

In all insolvency proceedings, it is essential to ensure a fair balance between the interests of the debtor's business and those of the relevant creditors. In order to ensure that the common interest of creditors is adequately protected (and, therefore, regardless of individual subjective positions that are protected based on the ranking of claims), almost all Member States provide for the establishment of committees representing creditors[315]. These committees are responsible for verifying that collective insolvency or restructuring proceedings are managed in a way that protects their interests and ensures the involvement of individual creditors, who might otherwise not participate in the proceedings due to their lack of importance in the decision-making process. Although creditors' committees are provided for in almost all Member States, the rules for them do

[315] The establishment of committees is left to the decision of the general meeting of creditors, which expresses its will, to the debtor or to the Court, to have its interests represented by such a committee. The establishment of such a committee has no purpose in the event that the insolvency office holder is able to adequately guarantee the interests of the creditors, and in all cases where participation of such a committee is not justified by the complexity of the procedure (e.g. in case of restructuring procedures regarding SMEs). ELI Instrument - Rescue of Business in Insolvency Law, Wessels, Madaus, Boon, 6 September 2017, paragraph 4.4.3, no. 438.

not appear to be standardized, either in terms of their constitution and composition, or in terms of their powers and voting rules.

Creditors can be a diverse group and creditors' committees can help make their interests heard in an insolvency proceeding, including minority creditors lending cross-border, as well as allow for decision-making. If given a proper mandate, a creditors' committee can help especially cross-border creditors exercise their rights and ensure their fair treatment, hence make cross-border lending more attractive. The role given to creditors' committees in an insolvency regime is directly linked with the roles attributed to other actors (courts, insolvency practitioners) – and ensure altogether the appropriate balance between the interests of creditors and debtors.

It is widely recognised that the interests of relevant creditors may be best served by coordinating their response to a debtor in financial difficulty through the establishment of (at least) one representative committee of creditors.[316] The establishment of such a committee is held to facilitate the active participation of creditors in insolvency proceedings, and to ensure fairness and integrity of proceedings.[317] Creditors' committees also contribute significantly to the supervision of the activity of the insolvency practitioner or so-called 'debtor in possession', considering the progress and quality of their work while at the same time avoiding wasteful interferences.

Rules relating to creditors' committees in insolvency proceedings are very different across Member States, these rules diverge as to the role attributed to the committees, the grounds for establishing them, their structure, form, powers, majority requirements etc.[318] These differences result in various levels of the actual input the creditors may have in the development of the insolvency procedure.

However, irrespective of any differences in individual national laws, an adequate participation of committees in insolvency and restructuring proceedings appears to be necessary for the purpose of maximising the recovery. At the same time, the participation of committees in proceedings should not hamper swiftness of the proceedings. In fact, being an instrument apt to guarantee one of the subjective positions involved, i.e. the creditors' position, its existence shall be adequately balanced with the other subjective positions involved and, more generally, with the effectiveness of the procedure. In this sense, it is worth mentioning that there are those rules that tend to exclude or limit the presence of such a body when the company is small and/or the number of creditors is limited. In such cases, the position of the creditors does not require any guarantee body, as it is already subject to protection by ordinary means.

Creditors' committees help find solutions that maximise the recovery value, but could give rise to hold out problems and delays. The existence of creditor committees widens the options of what can be done with the defaulted company, increasing the probability of remaining a going concern or selling assets at higher values to some creditors. Creditor

[316] Principles of European Insolvency Law (2003), Principle 2.4; see also INSOL International Workout Principles II (2017), Principle 4, and Asian Bankers Association's Workout Guidelines (2013) for informal workouts.
[317] UNCITRAL Legislative Guide (2004), Recommendation 129, and World Bank Principles (2016), Principle C7.1
[318] See mapping of these differences in Leeds Study, pp. 192.

committees allow creditors to cooperate, which is important given that multi-creditor lending relationships are common in the EU.[319] Negotiations with creditors can be costly for both the debtor and the insolvency practitioner tasked to liquidate a company.

Creditors may have different views about the best way forward, face collective action problems and can generate holdout problems that may prevent the insolvency practitioners from achieving an agreement that maximises the collective interest of all creditors. Foreign investors may feel disadvantaged by language barriers and unfamiliarity with the proceedings. Unless they hold a sizeable claim against the defaulting company, foreign creditors are likely to face information disadvantages and are less familiar with the position of other creditors, therewith face a higher threat of collusion. Well-specified rules are therefore important for them.

A further cost element originates from the activities required to recover some value from a defaulting investment, such as representation in a creditor committee and the bargaining with the debtor, other creditors and insolvency practitioners. Foreign lenders' lack of familiarity with the rules may also raise concerns about having one's interests adequately represented in the process. Representation in creditor committees is more costly for foreign investors and bargaining with other foreign creditors is more difficult for them.

Table A5.9 Rules and practices in EU Member States on creditors' committees

AT	A creditors' committee is not necessarily to be always appointed in insolvency proceedings. In some case is mandatory and in general where it seems advisable on account of the nature or the particular scale of the business. If the sale or lease of the business or part of the business is pending (Sec 117(1), number 1, AIA), a creditors' committee must always be appointed. It serves to supervise and assist the insolvency administrator (Sec 89(1) AIA). The administrator must consult the creditors' committee in respect of important arrangements (Sec 114(1) AIA). For certain important transactions (*e.g.* sale of the business), the consent of the creditors' committee is a precondition for validity. A creditors' committee consists of three to seven members. The appointment is made by the court of its own motion or on application. Not only creditors, but also other natural or legal persons may be appointed as members.	
BE	**General**	Creditors' committees are not defined. However, creditors influence certain aspects during proceedings as an assembly. For example, under Art. XX.37 of the BCEL, all creditors or at least two of them may accept the debtor's proposal to conclude an amicable agreement. They can also cast a vote upon the reorganization plan, in accordance with Arts. XX.67 to XX.83. of the BCEL.
	Voting rights	According to Art. XX.78 of the BCEL, '*the reorganization plan is deemed to have been approved by the creditors when it obtains the favourable vote of the majority of them, represented by their claims and half of all the sums due in principal (double majority).'* The creditor can take part in the vote in person, by written power of attorney, deposited in the register, or through their lawyer who can act without a special power of attorney. For the calculation of the majorities, the creditors and the amounts due appearing on the list of creditors filed by the debtor in accordance with article XX.77 (only the suspended creditors whose plan affects the rights can take part in the vote) are taken into account, as well as the creditors whose claims have subsequently been provisionally admitted in application of Articles XX.68 and XX.69. Creditors who did not take part in the vote and the claims they hold are not considered for the calculation of majorities.

[319] The analysis of bank data by Fell et al (2021) reveal that large firms have on average 2.7 lenders, medium size enterprises 2.5 and small firms on average 2.1. Moreover, their data shows that multi-bank credit relationships are overrepresented in non-performing loans.

BG	**Appointment**	According to Art. 672 of the BCA, the first meeting of creditors shall elect a creditors' committee comprising at least three and not more than nine members. The creditors' committee must comprise members who represent the secured and non-secured creditors, except those referred to in Article 616 2co of the Commerce Act. The creditors' committee duties are (Art 681 BCA): • to assist and supervises the actions of the receiver in relation to the management of the debtor's assets; • to conduct checks on the commercial records of the debtor and available cash funds; • to give opinions on the continuation of the business of the debtor's enterprise and on the remuneration of the provisional and ex officio receiver, the actions taken in relation to estate conversion into cash and on the liability of the receiver in other cases.
	Meeting of creditors	Under Art. 677 of the BCA, the meeting of creditors shall: • hear a report of the receiver in bankruptcy about his activities; • hear a report of the creditors' committee; • elect a receiver in bankruptcy, if none has been elected; in such case Art. 672, Para 2 shall apply; • pass a resolution for the removal of the receiver in bankruptcy and his substitution; • determine the amount of the current remuneration of the receiver in bankruptcy, any alteration thereof, as well as the amount of his final remuneration; • elect a creditors' committee, if none has been elected, or change its members; • propose to the court the amount of the support money for the debtor and his family; • determine the order and the way of conversion of the property of the debtor into cash, the method and terms for evaluation of the property, the choice of assessors and the determination of their remuneration.
	Meeting of creditors voting rights	According to Art, 676 BCA, the meeting of creditors shall be held, regardless of the number of persons present and shall be chaired by the judge responsible for the case. Resolutions shall be passed by simple majority, unless the law prescribes otherwise.
HR	**Appointment**	Creditors committee can be appointed by the court, prior to the first hearing of creditors. Creditors with the claims with in the highest amount and creditors with small claims must both be represented in the committee of creditors. Also, a representative of the debtor's former employees must be represented in the committee of creditors unless they as creditors participate in the proceedings with insignificant claims. Creditors with the right to seek separate satisfaction (*razlučni vjerovnici*) and persons who are not creditors, but who might contribute to the work of the committee with their expert knowledge, may be appointed members of the committee of creditors. The committee of creditors must have an odd number of members, nine at the most. If the number of creditors is less than five, all creditors are awarded the powers of the committee of creditors.
	Powers	The committee of creditors must oversee the liquidator and aid them in pursuit of business activities, as well as monitor operations pursuant to Article 217 of the CBL, examine the books and other records related to the business, and order verification of turnover and the amount of cash. Among its responsibilities, the committee can: • examine reports by the liquidator on the course of the bankruptcy proceedings and on the condition of the bankruptcy estate; • review business ledgers and the entire documentation that has been taken over by the liquidator; • lodge objections with the court against acts of the liquidator;

		• grant approval of the cost estimates for the bankruptcy proceedings; • give the court an opinion on liquidation of the debtor's assets, at the request of the court; • give the court an opinion on the continuation of ongoing business operations or on the activities of the debtor, at the request of the court; • give the court an opinion on recognition of justified losses that were established in the inventory of assets, at the request of the court.
CY	Creditors may appoint a '*supervisory committee'* if they wish to do so. There are certain actions for which the liquidator needs the permission from the court or from the supervisory committee, and there are some other actions that remain vested with the court (for instance the preparation of the contributors list, order a contributor to pay etc.). In addition, a board of creditors may vote upon the company's winding up during the voluntary winding-up by creditors procedure.	
CZ	**General**	Creditor bodies are: the creditors' meeting; the creditors' committee (or the creditors' representative).
	Creditors' meeting	The creditors' meeting is responsible for electing and removing members and alternate members of the creditors' committee (or a creditors' representative). The creditors' meeting may reserve for its competence anything falling within the remit of creditor bodies. If no creditors' committee or creditors' representative is appointed, the creditors' meeting acts in that capacity instead, unless otherwise provided by law. If more than 50 creditors are registered, the creditors' meeting must set up a creditors' committee. If it is not obliged to do this, a creditors' representative may take the place of the committee.
	Creditors' committee	The creditors' committee exercises the powers of creditor bodies, except in matters that are within the remit of the creditors' meeting or have been reserved by the creditors' meeting for its own competence. In particular, the creditors' committee supervises the insolvency practitioner's activities and is entitled to submit proposals to the insolvency court regarding the insolvency proceedings. The creditors' committee protects the common interest of creditors and, in cooperation with the insolvency practitioner, helps to achieve the purpose of the insolvency proceedings. The provisions on creditors' committees apply *mutatis mutandis* to creditors' representatives.
DK	In bankruptcy proceedings, a qualified minority of creditors may require the formation of a creditors' committee, consisting of up to three members. The insolvency court decides how the members of such a committee are to be elected, in order to ensure a diverse representation of the general body of creditors. The trustee must inform the creditors' committee of any significant actions taken and of any particularly significant actions that are planned to be taken, unless doing so would be detrimental for the estate. The creditors' committee is strictly of an advisory nature to the trustee and the insolvency court, and has no special powers. In addition, where a consensual restructuring is feasible, major creditors can form an ad hoc 'steering committee', as the success of the restructuring is dependent upon all creditors acceding to the restructuring plan.	
EE	Not *per se*. There is a general meeting of creditors, who participates in the conduct of bankruptcy proceedings The general meeting of creditors can decide to elect a '*bankruptcy committee'*. In accordance with BA, the bankruptcy committee shall protect the interests of all the creditors, monitor the activities of the trustee and perform other duties provided by law in bankruptcy proceedings.	
FI	**General**	The most important decision-making body is the creditors' meeting, but other decision-making procedures may also be applied. The court may appoint a committee of creditors to represent the creditors and to act as an advisory body to assist the insolvency practitioner in the performance of their duties.

		The committee represents all groups of creditors, and its duties are to assist the insolvency practitioner in the performance of their duties and to monitor the activities of the insolvency practitioner on behalf of the creditors. The committee makes its decisions by simple majority.
	Voting rights	Under Sec 52 of the Restructuring Act (RA), the restructuring programme is confirmed by a majority vote in each class of creditors. The programme may be confirmed even if minority creditors vote against it. Generally, a class of creditors is deemed to have approved the restructuring programme, if the programme is supported by: • more than 50% of the creditors that took part in the vote in a class of creditors; and • creditors representing more than 50% of the total monetary value of the claims represented in the vote for that class of creditors.
FR	Where the debtor has a workforce of more than 150 employees and turnover exceeding EUR 20 million, a creditors' committee is set up which will give its opinion on the draft plans to clear the liabilities. The court may also decide to apply these provisions below those thresholds. The creditors' committees convene different categories of creditors at separate meetings in order to submit to them proposals which they will be able to discuss and on which they will decide collectively, *i.e.* minority creditors will have to abide by the decision of majority creditors. There is a credit institutions committee composed of finance companies and credit or similar institutions, and a committee composed of the principal suppliers of goods or services. Where there are bondholders, a general meeting of all creditors holding bonds issued in France or abroad is convened in order to discuss the draft plan adopted by the creditors' committees. Creditors' committees must be consulted by the court-appointed administrator on the draft plan and vote in favour of a plan before the court can take its decision. Where creditors' committees exist, any creditor who is a member of a committee can propose alternatives to the draft plan presented by the debtor.	
DE	**General**	The Insolvency Code grants considerable influence over the insolvency proceedings to the creditors. The creditors exercise their rights through the creditors' meeting (Sections 74 et seq. GIC) or a creditors' committee (*Gläubigerausschuss*) that may optionally be set up by the creditors' meeting (Sections 68 et seq. GIC). Whereas the creditors' meeting is the central body through which the creditors take their decisions, the creditors' committee is a body through which they exercise supervision. The creditors' meeting is convened by the insolvency court (Section 74(1), first sentence, GIC), which also chairs it (Section 76(1) GIC). All preferred creditors, all ordinary creditors, the insolvency administrator, the members of the creditors' committee and the debtor are entitled to attend the creditors' meeting (Section 74(1), second sentence, GIC). If an enterprise exceeds certain size criteria, the insolvency court has to appoint a provisional creditors' committee even before the opening of the insolvency proceedings (Section 22a GIC). This committee is involved in the appointment of the insolvency administrator and plays a role in any decision on the ordering of debtor-in-possession management (Sections 56a and 270b(3) GIC).
	Voting rights creditors' meeting	Decisions of the creditors' meeting are in principle adopted by simple majority, with the majority being decided not by the number of votes, but by the sum of the claims held by the creditors voting (Section 76(2) GIC).
EL	**General**	Not existent.
	Voting rights	For creditors' meetings, in order to conclude an agreement on Pre-insolvency business recovery process, 50% consent of each category of creditors is required (secured and other claims), with the possibility of bypassing these majorities under certain conditions. Creditors' consent can also be provided through electronic voting.
HU	**General**	Creditors may form creditors' committees or elect a representative of the creditors with whom the liquidator must consult and whom the liquidator is obliged to inform and whose implicit or explicit consent must be obtained for certain measures. If the creditors have formed a creditors' committee the liquidator shall be required to obtain the consent of the committee for continuing business operations of the debtor. The same rule applies if the creditors have selected a creditors'

		representative.
	Voting rights	The liquidator may lease or transfer the debtor's assets only with the approval of the creditors 'committee or the creditors' representative or two-thirds of the creditors to a person or entity who, at the time of order of liquidation or within one year, was the executive officer of the debtor, or the debtor's sole or majority owner.
IE	Not existent. However, in certain liquidations there is a requirement for the creditors to form a committee of inspection which consists of representatives of the creditor group. The committee of inspection has a supervisory role (once reserved to the High Court) in the conduct of the liquidation and has the power to authorise certain acts of the liquidator and the liquidator's remuneration, costs and expenses.	
IT	The creditors' committee is composed of three or five creditors and appointed by the delegated judge, after hearing the curator and the creditors. The appointment is made within 30 days of the bankruptcy sentence, and within 10 days of the appointment the committee appoints the chairman. The creditors' committee performs: • Management functions: ✓ authorizes all acts of extraordinary administration to be carried out by the curator; ✓ authorizes the new curator to propose the action of responsibility against the revoked curator; ✓ authorizes the receiver to take over pending contracts in place of the bankrupt; ✓ approves the liquidation program presented by the liquidator. • Advisory functions: ✓ in all cases provided for by law (necessary advisory activity); ✓ when the court deems it appropriate (possible advisory activity). • Control functions: ✓ must endorse the register kept by the liquidator ; ✓ may make comments on the summary report on the activities carried out and drawn up every 6 months by the receiver; ✓ has the right to view any deed or document contained in the bankruptcy file; ✓ is informed by the receiver on the outcome of the sales carried out.	
LV	There is no creditors' committee. Other key players in insolvency proceedings in Latvia are the insolvency court (and the insolvency judge), the insolvency administrator, creditors acting at a creditors' meeting, the debtor's representative, the insolvency administration and the Latvian Association of Certified Administrators.	
LT	Creditors convene at a general assembly to decide on the establishment (and members) of the creditors' committee, to investigate any creditors' complaints regarding the conduct of the insolvency administrator, to request any reports from the insolvency administrator and to determine the level of the insolvency administrator's fees. The creditors' committee supervises the activities of the insolvency administrator and protects the interest of the creditors. Its rights and duties, as a general rule, are established by creditors as a whole at their general meeting.	
LU	**General**	On the basis of the debtor's proposed composition, the *juge délégué* issues a notice to attend to the creditors by means of a publication in the daily newspapers and by registered letter at least 8 days before the meeting is held. The *juge délégué* ensures that the composition procedure is carried out correctly and chairs the meeting of creditors. On the day of the meeting, the *juge délégué* reports on the state of the debtor's affairs. The debtor then presents the proposed scheme of composition directly to the creditors. The creditors are then invited to declare the amount of their claims in writing and to declare whether or not they agree to the composition. The composition may only be established with the approval of the majority of the creditors, representing 3/4 of the total claims accepted definitively or provisionally. A creditor may be represented by an authorised representative. Creditors who are unable to present themselves beforehand may submit any claims to the court clerk, along with the supporting documentation, during the week following the meeting of creditors and prior to the final deliberation meeting. They will then be required to accept or refuse the composition. Following the meeting of creditors, the court convenes another meeting in order to definitively approve the composition.
	Voting rights	A successful application requires the consent of a majority of creditors representing 75% of the outstanding debt. Creditors with claims which are secured

		by priority rights, mortgages or pledges can only vote if they waive those rights. The court will not ratify the application if the legal provisions are not met or for reasons of public interest or the interests of creditors. If the court deems that the conditions are not met, it declares the company bankrupt.
MT	No creditors' committee exists *per se*. A creditors' meeting does exists and has the following responsibilities. In a court winding up, creditors can make submissions to the court on the hearing of a winding-up application. In a creditors' voluntary winding up, following the resolution for winding up, the directors must call a meeting of the creditors and submit to them a full statement detailing the position of the company's affairs, together with a list of the company's creditors and the estimated amount of their claims. The creditors may also nominate the liquidator. If the creditors and the company nominate different persons, the person nominated by the creditors will be liquidator. The creditors may also form a liquidation committee. If the winding up continues for more than 12 months, the liquidator must summon a general meeting of the company and a meeting of the creditors at the end of the first 12-month period and each succeeding 12-month period, during which he or she must submit an account of his or her acts and dealings and the conduct of the winding up during the preceding 12 months, including a summary of receipts and expenditure.	
NL	If desired by the creditors, the court may nominate a committee of creditors to advise the trustee. However, the trustee is not bound by the committee's recommendations. In practice, the nomination of a creditors' committee is uncommon.	
PL	The participation of the creditors in the bankruptcy proceedings is governed by Articles 189-213 of the Bankruptcy Act. Creditors whose claims have been admitted are entitled to take part in the creditors' meeting and vote. The bankruptcy judge, acting *ex officio* or on request, establishes the creditors' committee and appoints and dismisses its members. The committee assists the receiver, controls his actions, examines the state of the funds forming the bankruptcy estate, grants permission for actions that may be performed only with the permission from the creditors' committee and expresses its opinion on other matters if requested by the bankruptcy judge or receiver. The creditors' committee may request the bankrupt party or the receiver to provide clarification and it may examine books and documents concerning the bankruptcy in so far as that does not infringe business confidentiality.	
PT	Once the insolvency proceedings are held open, the court shall appoint the members of a creditors' committee, comprising between three and five creditors representing different ranking claims, presided over by the debtor's major creditor. This committee shall cooperate with the insolvency administrator and is responsible for supervising the performance of the duties of the latter.	
RO	After the first meeting has been convened the delegated judge and then the creditors may appoint a creditors committee, which is made up, depending on the number of creditors, of three or five creditors from among those with the right to vote, with preference claims, budgetary claims and unsecured claims in order of value. The creditors' committee (*comitetul creditorilor*) has the following terms of reference: • to review the debtor's situation and to issue recommendations to the creditors' meeting with regard to the continuation of the debtor's business and proposed reorganisation plans; • to negotiate terms of appointment with the administrator or liquidator whom the creditors wish to see appointed by the court; • to take notice of the reports prepared by the court-appointed administrator or liquidator, to review them and, where applicable, to file objections thereto; • to prepare reports to be presented at the creditors' meeting in regard to the measures taken by the court-appointed administrator or liquidator and their effects, and to propose other measures, giving reasons; • to request the removal of the debtor's right to manage its affairs; • to file legal actions for the annulment of certain fraudulent acts or transactions performed by the debtor to the detriment of creditors when such legal actions have not been brought by the court-appointed administrator or liquidator.	

SK	**Duties and powers**	Committee's duties: • instructs and makes recommendations to the insolvency practitioner concerning managing the assets, running the debtor's enterprise or a part thereof, and realising the assets. This also includes hiring out the assets or a substantial part thereof (with restrictions when the enterprise is in operation). • concludes an agreement on the temporary provision of funds in connection with running the debtor's enterprise; • continues the running of the enterprise if the debtor is a particular type of financial institution; • establishing a lien on the debtor's assets; • concludes an agreement in connection with running the debtor's enterprise, in which the insolvency practitioner undertakes to continue performance beyond a particular time period or a particular percentage of turnover;
SI	The creditors' committee shall be formed: • in compulsory settlement proceedings, and; • in bankruptcy proceedings, if the formation of a creditors' committee is requested by the creditors. The number of members of the creditors' committee shall be determined by the court. The number of members of the creditors' committee must be odd and may not be less than three, unless the number of creditors is less than three, and not more than 11. In determining the number of members of the creditors' committee, the court must take into account the total number of creditors. The number of members of the creditors' committee shall be determined by the court: • if it is competent to decide on the appointment of the members of the creditors 'committee: by a decision appointing the creditors' committee, • if the members of the creditors' committee are elected by the creditors: by a decision on the election of the creditors' committee. In compulsory settlement proceedings, the court appoints the members of the creditors' committee by a decision on the institution of these proceedings. The court must appoint creditors as members who are the holders of ordinary claims against the debtor in highest total amount.	
ES	In general, creditors are represented in the creditors' committee, which will be considered validly constituted when the following quorum is reached: • claims for an amount of at least half of the ordinary aggregate liabilities; or • creditors who represent at least half of the class of claims that could be affected by the contents of the proposed Company Voluntary agreement (CVA).	
SE	In case of Business Reorganisation, the committee consists of no more than three members. In some cases, employees will also have the right to appoint a representative as an additional member of the committee. The court may appoint further members if there are particular grounds for doing so. The business reorganisation officer must consult the creditors' committee with regard to matters of importance if there is nothing to prevent this. In Bankruptcy the creditors have no formal role in the bankruptcy procedure. The administrator must consult creditors that are particularly affected if there is nothing to prevent this. The creditor are also entitled to receive information from the administrator, and to attend the taking of the oath, for example. A creditor may request that a supervisor be appointed to monitor the administration of the bankruptcy estate on the creditor's behalf.	

Source: Deloitte/Grimaldi (2022).

ANNEX 6: RECENT INSOLVENCY-RELATED REFORMS IN MEMBER STATES

Insolvency reforms in the Member States were often implemented in the context of either an economic adjustment programme or following targeted country specific recommendations in the European Semester context. The reforms described below extend beyond in-court corporate insolvency proceedings and in many cases also covers reforms to restructuring and out-of-court enforcement procedures.

1. Insolvency reforms introduced in the context of economic adjustment programmes of Greece, Portugal, Cyprus, Romania and Latvia[320].

In **Greece**, a series of legislative initiatives taken in 2015-2018 improved collateral auction procedures and introduced the option and, soon after that, the mandatory conduct of electronic auctions for foreclosures of movable and immovable property, while setting up a mechanism for out-of-court debt settlement for indebted businesses and professionals, with limited results[321]. Given that the actual implementation of foreclosures and insolvency procedures remained fragmentary and complicated and the relevant conduct of judiciary procedures overly lengthy, a new integrated corporate and personal insolvency framework was adopted in October 2020 and fully entered into force in June 2021. Pre-bankruptcy proceedings are available under the new code, including an automated out of court process and a prepack business recovery process contingent to court ratification. The platforms under the new insolvency framework have started gradually bearing results, particularly with respect to out-of-court settlements and further improvements are continuously being developed.

In **Portugal**, the amendment of the insolvency law was introduced in spring 2012. Later in the year, both in-court fast-track mechanisms and out-of-court tools were made operational to facilitate the solution of the insolvency cases. However, the insolvency framework required further amendments to improve the corporates' rescue and restructuring process. As a result, it was followed-up in the European Semester process: Portugal has received country specific recommendations (CSRs) linked to these issues (2014, 2017, 2018, 2019), following its exit from the Programme. As a consequence, further amendments have been introduced in the insolvency framework. In 2017, the use of electronic means was broadened, while the possibility of creditors to choose the insolvency practitioner was restricted to complex cases. In 2022, Law 9/2022 was adopted in January and entered into force in April, which aims at simplifying the insolvency and civil enforcement judicial procedures. The amendments to the insolvency code, in particular, are expected to simplify the processing of verification and ranking of creditor claims. Furthermore, the creditor rights will be strengthened with the revision of the preferential regime for the right of retention in relation to mortgage credit. Other

[320] In the case of Romania and Latvia, reforms were enacted in the context of the Balance of payments assistance programmes of 2013-2015 and 2009-2011 respectively.

[321] In parallel, various amendments were introduced throughout the Greek programs to the problematic personal insolvency law, which was initially adopted in 2010 with the intention to enable the restructuring of personal debt and protect vulnerable primary residence owners but resulted in procedural abuses by strategic defaulters.

legislative procedures are also scheduled to enter into force in the coming months and are expected to streamline and speed up insolvency processes in Portugal. The revision of the legal framework for insolvency and recovery forms also part of a wider reform envisaged under the country's national Recovery and Resilience Plan.

In **Cyprus**, a legislative package with regard to the insolvency and foreclosure procedures was introduced in 2015 but once again, amendments were required. As a result, a new legislative package was introduced in July 2018 in order to make the measures more effective. E-auctions were introduced in 2019 but additional amendments, which were introduced in 2019 and entered into force in 2020, may create some delays in the foreclosure process for new NPLs. The need for further improvements was also reflected in the CSRs received by Cyprus following its exit from the program in 2016, 2017 and 2018. More recently, the Recovery and Resilience Plan of Cyprus has included a reform to reinforce and strengthen the insolvency framework by enhancing the functionality of existing systems and introducing new ones in order to create efficiencies through automation.

Romania adopted a new law regarding insolvency and bankruptcy in June 2014 while in May 2015 a new personal insolvency law was introduced, which entered into force in December 2015, drawing upon good international practices and including more balanced provisions for both debtors and creditors.

In **Latvia**, a new insolvency law came into force in 2010, concerning both legal and natural persons, following international best practices. The law was further amended in 2015, in an effort to reduce the length of insolvency proceedings, when electronic auctions were introduced. A revision in the legal framework in 2016 aimed at improving the accountability and public oversight of insolvency administrators, in line with country specific recommendations (CSRs) received by Latvia in the period 2013-2015, following its exit from the balance of payments assistance program.

2. Insolvency reforms introduced in the European Semester context

The push for streamlining insolvency procedures has not been associated only with countries under a macroeconomic adjustment program. Several countries facing challenges with their stock of non-performing loans received **country specific recommendations** (CSRs) in the past to expressly enhance the efficiency and speed of their insolvency and recovery proceedings and facilitate debt restructuring and/or out-of-court settlement. Apart from countries already mentioned above, these included Croatia (2014, 2015), Bulgaria (2014-2018, 2020), Italy (2016-2018[322]), Slovenia (2013, 2014), Spain (2013, 2014) and Hungary (2014), without taking into account CSRs referring to the need to enhance the efficiency of the judicial system as a whole. This has led to certain insolvency reforms being implemented in many of these Member States. For example:

- In **Croatia** the Bankruptcy Act (BA) is the main law governing the insolvency of businesses (including individual entrepreneurs) in Croatia and came into force in

[322] A reference to insolvency is also included in the 2019 CSR4 for Italy: "Reduce the length of civil trials at all instances by enforcing and streamlining procedural rules, including those under consideration by the legislator and with a special focus on insolvency regimes.[…]"

2015. The adopted BA also improved the pre-insolvency procedure. More recently, the Recovery and Resilience Plan of Croatia has included a reform to amend in 2022 the Bankruptcy Act and the Consumer Insolvency Act with the aim to ensure greater efficiency of insolvency proceedings.

- **Bulgaria** has introduced new legislation on business restructuring which entered into force on 1 July 2017, although some important elements remain missing. To tackle with those, a Roadmap on the insolvency and stabilisation framework for bankruptcy was adopted in June 2019, aiming for an amendment of the Commercial Law and the relevant by-laws[323]. However, the work on the legislative amendments to the Commercial Act and other relevant primary and secondary legislation in line with the requirements of Directive (EC) 2019/1023 is still ongoing. The Bulgarian authorities have committed to complete this reform by July 2022, in line with Bulgaria's commitments following its ERM II entry. This has also been reflected as a distinct reform in the country's national Recovery and Resilience Plan.

- **Slovenia** completed the reform of its insolvency framework in 2014, allowing more *restructuring* opportunities to companies in financial difficulties.

- **Hungary** reformed its personal insolvency legislation in 2015 in order to address the issue of personal over-indebtedness and to protect the home of indebted persons from enforcement.

- In **Italy**, alternative in-court and out-of-court workout arrangements had been introduced over the previous years, with a rather muted impact. The government finalised in early 2019 the reform of the insolvency framework but its entry into force was postponed to 2022 due to the impact of the pandemic. Further improvements in the insolvency framework were incorporated as a deliverable under the Italian Recovery and Resilience Plan, following a staggered approach. A new out-of-court settlement arrangement was introduced, the so called "Composizione negoziata". The new arrangement introduces the possibility for the entrepreneur to use an independent expert to propose a negotiated procedure with creditors. Moreover, between August and December 2021, Italy took various legislative and administrative decisions to flank the new out-of-court settlement arrangement. As a result, an online platform for the out-of-court resolution of disputes was put in place in November 2021, allowing exchanges of documents between debtors and creditors, and pre-approved automated restructuring procedures were introduced for debts below EUR 30.000.

- Because of the financial crisis, **Spain** reformed its bankruptcy code four times (once in 2009, once in 2012 and twice in 2014) with the aim of decreasing the duration of bankruptcy procedures and increasing the percentage of successful reorganisations. In 2015 another reform of the code was approved with the purpose of solving the over-indebtedness problems of individuals, by granting them a second chance by

[323] The planned legislative changes included the introduction of early warning systems for businesses and debt forgiveness procedures for entrepreneurs, easy and fast access to insolvency proceedings, stabilisation procedures for legal entities and entrepreneurs, accelerated procedures for small businesses and shortened procedural deadlines in the insolvency proceedings.

means of the cancellation of the debts that they are unable to pay if some requirements are met. More recently, Spain has included in its national Recovery and Resilience Plan further changes to the Insolvency Law, to be completed in 2022, which aim to set-up a more efficient second chance procedure for natural persons, allowing for debt relief without prior liquidation of the insolvent party's assets, and at the same time establish a swifter and more cost-efficient special procedure for micro SMEs, fully processed by electronic means.

- **Malta**[324] reformed its insolvency legal framework in 2017 in order to reduce the costs and duration of relevant procedures and increase the availability of qualified practitioners. It adopted legislative measures to facilitate company restructurings, allowed for a Second Chance for honest directors who have concurred with the law and introduced voluntary mediation procedures in insolvency, so that professional mediators could amicably resolve matters, if agreed by at least 60% of the companies' creditors. There are also legislative measures to facilitate company restructurings.

3. Insolvency reforms announced in introduced in Member States' Recovery and Resilience Plans

The table below lists what Member States committed to undertake in the area of insolvency in their recovery and resilience plans. Many of the reform elements relate to the transposition of the Restructuring Directive (EU 2019/1023), the creation of early warning tools, out-of-court procedures and areas out of scope of the EU initiative such as regulation of insolvency practitioners and specialisation of courts. The right-hand column informs about reform measures that cover items in direction of the measures pursued with this initiative.

	Measures outside the scope of the targeted harmonisation	**Measures in a similar direction**
BG	Transposition of Directive (EU) 2019/1023, provide for stricter regulation of the profession of insolvency practitioners, early warning tools, legal guarantees for traders to register the actual management addresses when registering companies.	Use of electronic means in insolvency, restructuring and discharge of debt procedures, duties of the directors in case of likelihood of insolvency
EL	Upgrade of the early warning and the preventive debt restructuring mechanism	Digitalisation
ES	A more efficient second chance procedure for natural persons, allowing for debt relief without prior liquidation of the insolvent party's assets, restructuring plans as a new pre-insolvency instrument	Establish a special procedure for micro SMEs
HR	Amendments to the Bankruptcy Act and the Consumer Insolvency Act which shall ensure greater efficiency of insolvency proceedings, improve the system of organization and appointment of insolvency practitioners and supervision of the performance of the service,	Amendment of Article 212 of the Bankruptcy Act relating to avoidance proceedings

[324] Malta received in 2013 a Country Specific Recommendation on the overall efficiency of the judicial system, which included, for example, a reference to the need for speedier resolution of insolvency cases.

	implement Directive (EU) 2019/1023 (Restructuring Directive)	
IT	Review out-of-court settlement arrangements; put in place early warning mechanisms and access to information prior to the insolvency phase; shift towards specialisation of courts (commercial law, insolvency division/chamber) as well as pre-court institutions to manage insolvency proceedings in insolvency; allow secured creditors to be paid first (before tax claims and employee claims); allow businesses to grant a non-possessory security right.	Digitalisation of restructuring and insolvency proceedings
CY	Modernising the Cyprus Companies Law by using best practices from other common law jurisdictions, the law review shall include the insolvency proceedings under the Companies Law, which are Liquidations, Receivership and Examinership.	
LT	A digital tool (a wizard) helping to draw up a restructuring plan of a company	Insolvency portal, a digital tool (a wizard) helping in the process of asset valuation to apply international valuation standards by providing best practices, examples and explanations in one place; a tool to perform comparisons of asset and transaction valuation
PT	In and out-of-court settlements, legal framework for voluntary administrative arbitrage, and the creation of specialised chambers in superior courts, review of the legal framework strengthening the rights of the lender, and introduce compulsory partial apportionment in specific cases	Establishment of purely electronic proceedings strengthening of the role of insolvency practitioners
SK	Early warning tools and specialisation in business courts	Digitalisation

ANNEX 7: SME TEST

1. Identification of affected business	
SMEs are within the scope of this legislative initiative and would be impacted directly and indirectly since they face a hightened risk of failure, which may lead to a business being wound down through an insolvency procedure. SMEs constitute a large part of the enterprise population and have a higher exit rate than larger enterprises. The discrepancy between exit and insolvency statistics, which are sourced from different reporting entities, suggest that only a small share of business exits are due to insolvency and this is likely also the case for SMEs. For example, the large number of business exits of firms that have no employee suggests that many firm are closed because the entrepreneur found employment or the firm had fulfilled its function. While data on SMEs as subjects of insolvency proceedings is scarce, the available observations from Member States suggest that 80 to 95% of all insolvency cases concern entities with fewer than 10 employees (data from DE, ES, FR and SE). 99.5% of insolvency cases in France concern SME if the definition of a firm with less than 250 employees is used, 100% in Sweden. For other Member States, the number could not be found	Problems (2.12), drivers (2.3.2) and options (5.2)
2. Consultation of SME Stakeholders	
Efforts have been made to consult SMEs (and insolvency experts well-acquainted with their situation) through the consultation and study. Specific outreach to SMEs was not done as this was considered too time-consuming in the light of very little, if any, negative impacts expected and positive impacts materialising for resource-strained SMEs that are in the process of business exit, which would likely not have capacity to interact with the Commission services. Only one business association that represents SME interests participated in the public consultation. It expressed the status quo as representing a problem that warranted policy action and flagged most of the issues addressed through this initiative as obstacles (rating of 5 on a scale 0 to 5). The submission of this association was more supportive to the initiative than those of other business associations. Another business association that represents business at large, including many SMEs was less critical on the status quo and the need for policy action, but emphasised it would "favour of a sound insolvency framework that strengthens the position of SMEs regarding recovery." The low participation of SMEs in the consultation could also to some degree be interpreted as a sign that SMEs generally have little or no (sophisticated) knowledge of insolvency proceedings since their details and complexities exceed their capacities to assess burden and costs and most currently do not make use of such procedings. The smaller a company the more cumbersome insolvency proceedings become and the proposal to introduce a specific insolvency regime for MSEs aims to address this issue. Since this proposal for an MSE regime was developed at a rather late stage, it did not feature in the public consultation. Members of the Expert Group with experience on SME insolvencies however supported this element.	Stakeholders' perspective (section 2.1.3)

3. Assessment of the impact on SMEs	
The conditions under which SMEs are wound down has an impact on their recovery value as gone concern as well as on their financing conditions and their capacity to build business relationships when solvent. The initiative would primarily improve the business environment for SMEs. By increasing expected recovery rates for creditors exposed to SMEs and other businesses, the initiative would reduce perceived risk of investing in SMEs, which is expected to be reflected in lower funding costs for SMEs, ceteris paribus. Meanhile, the initiative does not impose obligations or compliance costs for SMEs that are economically active and simplifies procedures for those who face insolvency. Entrepreneurs would benefit from a quicker realisation of a second chance, i.e. to be discharged from the debts of the previous undertaking and make a fresh start. The cross-border dimension related to access to funding from non-domestic sources is likely to be relevant for only some SMEs. Foreign creditors invest in small firms only rarely and tend to focus on innovative enterprises with high growth potential. While debt issuance of medium-sized firm is negligible, some issue shares, which are also held by foreign investors, which take into consideration how the firm is wound down when deciding on their investment. The initiative aims to introduce a special procedure for MSEs to facilitate and speed up their winding down. This would lower judicial costs and shorten the time for the second chance. The MSE regime would moreover support the orderly winding down of "asset-less" MSEs, addressing the issue that some Member States reject access to an insolvency proceeding if the projected recovery value is below the judicial costs. The impact assessment used SME specific information to the extent they were available, for example recovery rates, time and judicial costs of SME loans from the EBA benchmark exercise and indications by insolvency practitioners about the cost savings of an MSE insolvency regime. Specific analysis covers the benefits and costs of such a dedicated insolvency regime for MSEs. It finds that cost savings for insolvent SMEs are 12% according to the survey for those that have access to insolvency proceedings. While the possibility for asset-less MSEs to access insolvency proceedings will be beneficial, it can entail costs for the public sector, for which a range was estimated using a number of assumptions.	Impacts (sections 6.1.2, 6.13 and 6.2.3, annex 4 [section on MSE loans])
4. Minimising negative impacts on SMEs	
The absence of compliance costs and the overall beneficial effects for SMEs made it unnecessary to design mitigating measures for SMEs	

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