Restructuring and insolvency in Luxembourg (part 2)

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RESTRUCTURING - COURT PROCEDURES

Formal, court-driven restructuring proceedings are available into Luxembourg law, but for practical reasons, these are rarely used in practice.

Reprieve from payment procedure (*sursis de paiement*)

The reprieve from payment procedure allows a debtor to restructure its debt with the consent of a majority of its creditors outside of insolvency proceedings. Its purpose is to allow a business experiencing financial difficulties to suspend its payments for a limited period of time. The reprieve of payment has to be approved by creditors representing 75% of all the outstanding amounts. For the purpose of calculating the required majority, those claims that are secured by rights of priority, mortgages or pledges, as well as the tax claims and other public charges are not taken into consideration.

The reprieve (ie. *suspension of payments*) may only be granted by the court:

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During the period of time the reprieve from payment is in force, the debtor loses the right to manage solely its assets and is only allowed to manage its business under the control of a court-appointed commissioner (*commissaire*).

In practice, this proceedings are rarely used.

Composition to avoid insolvency (*Concordat préventif de faillite*)

A composition is an agreement between a company experiencing financial difficulties and its creditors under the control and with the approval of the court in order to avoid insolvency. Such agreement may include:

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The proposal must have the support of a majority of the creditors representing by way of unchallenged or provisionally accepted claims, 75% of the outstanding amount. The creditors having claims secured by rights of priority, mortgages or pledges may only vote if they waive such rights. After the creditors' approval, the court takes a decision with respect to the composition on the basis of a report that is presented by the appointed judge. The court will then verify whether the applicant is unfortunate and acting in good faith, whether the proposal for the composition is serious and appears to be realistic and whether the required approval threshold in number and in value has been reached.

The ratification of the composition will have no effect on the creditors who did not participate in the composition proceedings and did not, therefore, waive their rights of priority, their mortgages or pledges. These creditors may continue to act against the debtor in order to obtain payment of their claims and they may enforce their rights, obtain attachments and obtain the sale of the assets securing their claims. The ratified composition is only binding on the creditors existing at the date of the composition.

Controlled management (*gestion contrôlée*)

Controlled management is a benefit (seen as a privilege) granted by the court to protect a company which has suffered an impaired creditworthiness or which has difficulties in meeting all of its commitments when due from creditors wishing to take enforcement measures. The purpose is to assist the company either to reorganise its business or to convert its assets into cash under the supervision of the court and of the commissioners appointed by the court and with the approval of the creditors.

If the court accepts the application made by the distressed company, it assigns a judge to prepare

a report on the financial situation of the company. The assignment of the judge prevents creditors from enforcing claims or court decisions against the applicant, although creditors may still commence or continue court proceedings against it. At the same time, the applicant loses the right to dispose of, pledge, or mortgage its assets or enter into contracts without the judge's authorisation. Acts that have not been authorised as required are null and void.

During the entire court procedure, secured and unsecured creditors may not enforce against the debtor.
The plan must be approved by more than 50% in number of the creditors representing more than 50% in value of the debtor's liabilities. Even if the plan has received the necessary number of votes, the court may refuse to approve it. Once approved, the plan becomes binding on all creditors, co-debtors, guarantors, and the applicant. If the company does not perform its obligations under the plan, any creditor may institute court proceedings for cancellation. The court will then decide whether to terminate the plan and declare the company bankrupt.

Foreign restructuring procedures

Moving the centre of main interest (**COMI**) of a company to the UK in order to avail of certain English law restructuring procedures (including the pre-pack sale and the scheme of arrangement) which are considered as more practicable than those available in Luxembourg has become an alternative for debt restructuring. While such relocation could be a relative straight-forward process when involving a holding company, relocating the COMI of an operating company to the UK, if at all possible, may well involve physically moving the headquarters and employees and effectively require a degree of agreement from the main creditors.

An English scheme of arrangement may also be available to an overseas company irrespective of where its COMI is located. Sufficient connection to England will suffice. This may often be the case in leveraged buyout transactions with sufficient nexus to English law.

One of the main advantages of a scheme of arrangement is that it can be used by a company to restructure its debts without the need for unanimity in circumstances where this would otherwise be required under the terms of the relevant credit documentation. For a scheme of arrangement to become effective, it has to be approved at a meeting of the creditors, or in separate meetings of different classes of creditors, by at least 75% in value and a majority in number of those registering a vote on the scheme and then be sanctioned by the English court, which can be of greater use than the currently available Luxembourg law options.

LUXEMBOURG BANKRUPTCY PROCEEDINGS

Commencement

Under Luxembourg law, a company is considered insolvent when (a) it ceasing to pay its obligations and (b) its creditworthiness is impaired. It means in practice that no cash is available to the company to discharge its substantive obligations and it is not able to access further financing.

Insolvency proceedings (*faillite*) can be initiated either by the company itself, by the court of the district where its registered office is located, or by a creditor of the company. When initiated by the company itself, the insolvency petition must be made within one month of becoming insolvent.

On granting the petition, the court will appoint a receiver (*curateur*) in charge of the liquidation and a judge (*juge commissaire*) to supervise the proceedings. It will also determine the date on which the company is considered to have ceased to make payments in discharge of its obligations.

The receiver administrates the winding-up of the insolvent company. He realises the assets of the insolvent company and liquidates its debts under the supervision of the supervisory judge. The receiver acts in the best interest of the creditors.

Effects

An insolvency judgement has the effect of stopping all attachment or garnishment proceedings brought by unsecured or non-privileged creditors.

However, the stay of enforcement does not apply to Luxembourg law security interests (like pledges) governed by the Luxembourg law on financial collateral arrangements. A vendor can also retain title in contract (and therefore retain possession) of the assets until he receives payment (similar to the English law position on retention of title). Finally, if a creditor holds a mortgage and has begun proceedings to seize the property, the receiver may order an end to the proceedings and sell the property, distributing the proceeds to creditors with claims secured by the mortgage. If the proceeds from the sale are insufficient to reimburse the secured creditors, then they are treated as unsecured creditors with respect to the balance of their claims. As previously mentioned, certain transactions carried-out during the “suspect period” may be vulnerable to be declared void on application to the court. Again such rules are disapplied for certain Luxembourg law security interests (like pledges) governed by the Luxembourg law on financial collateral arrangements.

Recognition of Foreign Insolvency Proceedings

Luxembourg courts will not recognize foreign insolvency proceedings targeted at companies or branches domiciled in Luxembourg, except in the following exceptional circumstances:

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Similarly, Luxembourg courts will not exercise jurisdiction over proceedings aimed at companies domiciled outside of Luxembourg except in one of the above situations is met, or if the foreign defendant does not challenge the Luxembourg court's jurisdiction.

EU Cross-border Insolvency

Pursuant to the EU Council Regulation on insolvency proceedings (the **Regulation**) the courts of the EU member state in which territory the debtor's COMI is situated shall have jurisdiction in insolvency proceedings. In the case of a company or other legal person, the place of the registered office shall be presumed to be the centre of its main interests, subject to any proof to the contrary.

The judgement opening the proceedings shall, with no further formalities, produce same effects in any other member state as under the law of the state of the proceedings.

If the debtor's COMI is situated within the territory of one member state, the courts of an other member state shall only have jurisdiction to open insolvency proceedings against that debtor, if he possesses an establishment within the territory of that other member state. The effects of those proceedings (secondary proceedings) shall be restricted to the assets of the debtor situated in the territory of that other member state.

Current reform proposals

Draft legislation on business preservation and modernisation of bankruptcy law was introduced in the Luxembourg Parliament/Legislator on 1 February 2013.

Beside extra-judicial procedures aiming to avoid formal insolvency proceedings (appointment of a mediator, procedural framework for mutual agreement with some creditors), the draft legislation propose to introduce the possibility of a moratorium in order to reach either:

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These measures aim to replace the existing procedures such as the scheme of composition with creditors, controlled management and the suspension of payments given the practical challenges associated with them in a modern business context.

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