

Reform 3/2009 to the Spanish Insolvency Law

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The Royal Decree Law 3/2009 of the 27th of March is a recent reform of the principal Spanish rules relating to insolvencies, i.e. the Insolvency Law 22/2003 of the 9th of July.

The principal Spanish rules relating to insolvencies are found in the relatively recent Insolvency Law 22/2003 of the 9th of July, approved in a moment of economic prosperity. This law has been the object of a recent reform, by way of the Royal Decree Law 3/2009 of the 27th of March, driven in part by the current global economic crisis. This law has been affected by the current global economic crisis like the Spanish economy has been affected. The circumstances in which this law has taken effect are very different from the economic times in which the Insolvency Law was approved. On the other hand, the application of the Insolvency Law during these six years of validity has allowed the Insolvency Law's principal deficiencies to surface, some of which the new reform has tried to modify.

The executed reform focuses on three objectives: (i) to facilitate the refinancing of companies that have encountered financial difficulties independently from insolvency proceedings, where such financial difficulties do not make an insolvent situation unavoidable, (ii) to expedite the steps of the process, trying to reduce the costs of the total process, (iii) to improve the judicial position of the employees of companies in insolvency proceedings, who are affected by the collective procedures. Also, two important new concepts are introduced: an additional time period is allowed for negotiating an agreement of the creditors in advance, and newly determined concepts of the subordination of credits is also introduced in this reform.

The object of this article is to make reference, in a succinct manner, to only to those issues that we understand to be the most relevant of the reform. To this end we have included the following sections with the most significant measures of this Law:

- 1.) To facilitate the refinancing of those companies with financial difficulties.
- 2.) The introduction of an additional time period before the insolvency proceeding with the objective to negotiate an agreement of the creditors in advance.
- 3.) To expedite those steps of the process, trying to reduce the costs of the total process.
- 4.) To improve the judicial position of those employees of companies in insolvency proceedings, who are affected by the collective procedures.

We proceed to address each of these points:

- 1) To facilitate the refinancing of those companies with financial difficulties.

The Spanish Insolvency Law establishes an important rule of cancellation of those acts that are harmful to the creditors' interests. According to article 71, when the insolvency proceeding is declared, those acts that are harmful to the creditors' interest will be able to be cancelled when caused by the debtor within the two years prior to the date of the declaration of the insolvency proceeding, even though a fraudulent intention did not exist.

This principle establishes a series of presumptions, among which we stress that except with a proof showing to the contrary, it is presumed that damage to the creditors' interest has occurred in the cases where real guarantees are formed in favour of pre-existing obligations, or when new guarantees are formed to substitute those made for pre-existing obligations. Even though this situation is only a presumption, and a showing to the contrary is permitted, such a showing in some occasions may be a complex issue.

Practice showed that certain refinancing operations involve several risk, damaging banks and other such entities, and lastly causing damage to the debtor, whose refinancing could be denied. Application of this principle to an operation of refinancing of debt means that there could be a cancellation of a real guarantee, for example, a mortgage. Such cancellation would guarantee newly formed obligations that substitute the former ones in a refinancing process. The judicial insecurity that this situation could provoke was very significant.

With this deficiency in mind, the current reform establishes that those agreements of refinancing, like those of business, acts and payments made and guarantees established in the execution of such agreements, will not be subject to the principle of cancellation, always when these requirements are met: (i) that the agreement is signed by those creditors whose credits represent at least three-fifths of the amount due by the debtor, (ii) that the agreement contains information provided by an independent expert, and (iii) that the agreement is formalized in a public document.

Along with the exception of the application of the cancellation principle, there exists another exception. The second exception involves those guarantees that not able to be cancelled when such guarantees are made in favour of credits of public right, and in favour of the Fund of Salary Guarantee in those agreements of recuperation seen in the specific rules.

- 2) The introduction of an additional time period before the insolvency proceeding with the objective to negotiate an agreement of the creditors in advance

To understand this modification it is necessary to briefly mention that in the Insolvency Law it is established that the debtor has a duty to solicit the declaration of an insolvency proceeding within the two months following the date when the debtor knew or should have known of its insolvent situation. A short time period is established to protect the creditors as the end in mind. The creditors' non-compliance may have serious consequences, among other issues, relating to the responsibility of the debtor's administrators.

The reform allows the short time period to be flexible. Such time period will not be necessary for the debtor who has initiated negotiations to obtain acceptances for a proposal of agreement with the creditors within the time period of the two months previously indicated, when the debtor makes such circumstances known to the court. After three months have passed from the date of such communication to the court, the debtor, regardless of whether it has obtained the acceptances necessary for the admission of the proposal of agreement in advance, must solicit the declaration of the insolvency proceeding within the following month.

Some type of action by the debtor within the time period of two months continues to be necessary. In this case, the action necessary will be the communication to the court, and those negotiations with creditors with the objective to try to reach a proposal of agreement in advance. Nevertheless, in practice, the introduction of this time period may imply an additional extended time period of three months to solicit the declaration of the insolvency proceeding.

- 3) To expedite those steps of the process, trying to reduce the costs of the total process

The Insolvency Law establishes two types of procedure: the ordinary and the abbreviated. The abbreviated procedure involves a more flexible and less costly process, provided that the procedural time periods are decreased to half of what it would be, and names only one insolvency proceeding administrator in front of three administrators. With the reform it is established that those insolvency proceedings whose initial estimation of debt owed does not exceed 10 million euros, always when the other legal requirements are met, will be able to be processed by way of the abbreviated procedure. The previous regulation had a limit of 1 million euros. In practice, this means that a great number of insolvency proceedings that before should have been processed by means of the ordinary procedure can now be processed using the abbreviated procedure, enjoying the advantages of the cost and time that the abbreviated procedure implies.

Additionally, a system of advertising the announcement of the resolutions of the insolvency proceeding is established. The Public Register of Insolvency Proceeding Resolutions is recently established to regulate this system. This registry facilitates the advertising of insolvency proceeding resolutions, which can be accessed by anyone without a fee in the internet.

The possibility to solicit an anticipated liquidation of a company is also established. More clearly, such liquidation can be applied for during the first phase of the insolvency proceeding (the common phase) without waiting for the termination of those incidents that may arise in those insolvency proceedings relating to the challenge of the inventory list and of the list of creditors.

Finally, referring back to those new concepts that are most significant in the expedition and reduction of the insolvency procedure, we stress the new regulation of the retribution of the insolvency proceeding administrators. On the one hand, such retribution is reduced, and on the other hand, a guarantee of retribution is introduced in such a way that those cases in which the amount owed is insufficient, the payment of a minimum amount of retribution will be guaranteed. This guaranteed minimum amount of retribution will be provided with contributions of those insolvency proceeding administrators in other proceedings.

4) To improve the judicial position of those employees of companies involved in insolvency proceedings, who are affected by collective procedures

To better understand this newly established concept, it is convenient to briefly reflect on the Insolvency Law. According to the Insolvency Law, a substantial modification of the employment conditions and extinction or collective suspension of the employment contracts is able to be requested from the Judge only when the insolvency proceeding administration report is given. This report is delivered within the common phase of the insolvency proceeding, and those insolvency proceeding administrators must present it within a time period of two months from its acceptance. This situation may involve, in practice, a relatively long period of time from when the application for the declaration of the insolvency proceeding is presented, providing that it is necessary in the first place that the Judge produces a decision declaring the insolvency proceeding and the insolvency proceeding administrators give their acceptance to their appointment as administrators. In practice, after the Insolvency Law became effective, it was relatively common that the debtor had to wait for several months from the presentation of the application of the declaration of the insolvency proceeding before being able to initiate the process of substantial modification of employment conditions and the extinction or collective suspension of employment contracts. Despite that which has already been indicated, an exception was established in which the previously mentioned modifications could be solicited if it was found that a delay in the application for the mentioned modifications could seriously threaten the future viability of the company.

With the current reform the indicated exception is expanded, allowing the previously mentioned modifications to be adopted not only when it is found that the delay in the application could seriously threaten the future viability of the company, but also when serious damage could be caused to employees. This expansion of the exception attempts to protect employees that could find themselves in damaging situations due to an insolvency proceeding.

We can conclude that the reform mentioned here has imposed important advances, especially relating to refinancing operations in the areas of simplification and expedition of its corresponding procedures. Nevertheless, it had to have been an innovative reform that gave way to a more significant expedition of the processing and improvement of the current procedure, which, in many cases, causes important delays in practice.

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