Country Reports

Latvia, France & Spain

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Latvia

New Latvian insolvency law brings more reforms

On 1 November 2010, the new Latvian Insolvency Law took effect and many have already reacted to it as somewhat revolutionary. Although previous vital changes in the insolvency field were made hardly two years ago, the financial and economic crisis has highlighted several problems and drawbacks in the insolvency procedure. The new law is expected to lead to easier access to insolvency and restructuring procedures, help raise efficiency of insolvency administrator's work, and considerably quicken the procedure for selling debtor's possessions.

Dropping the balance sheet test for legal persons

The new law introduced several essential changes to insolvency proceedings. The minimum default debt allowing limited liability companies and joint stock companies to apply for insolvency has been raised to approx. EUR 4,300.

In future, courts will apply only the so-called "liquidity or cash flow test" and check the existence of debt and default. The law lifts the previous "balance sheet test" that made the courts assess whether assets exceed obligations, which meant that initiating insolvency proceedings could sometimes be significantly deferred.

The law will now allow creditors to withdraw an insolvency application, for instance, where the debtor has repaid the debt. This provision might create a risk of using insolvency proceedings as a method of debt recovery. However, two novel aspects might deter this kind of misuse. Firstly, a person filing a bankruptcy application must pay a deposit of two minimum monthly salaries (at present approx. EUR 500). Secondly, a petitioning creditor will have to repay amounts received from a debtor during the last three months to avoid insolvency on the basis of that creditor's application.

Restructuring process can become longer

The Insolvency Law will bring many novelties in restructuring or so-called legal protection proceedings (LPP) and out-of-court legal protection proceedings (OLPP).

Firstly, practical solutions to economic problems will become more important than compliance with formalistic requirements. For example, a debtor is now required to submit a forecast regarding income, as well as a cash flow projection.

Secondly, the maximum term of restructuring will be four years. In practice this increases the possibility of successful restructuring because in many cases only two years was too short for restoration of solvency.

Thirdly, from now on the most important decisions in LPP and OLPP (such as approval of the plan and choice of an administrator) requires approval by both two thirds of secured creditors and a half of unsecured creditors.

"Second chance" for private individuals

The insolvency process for private individuals, which caused extensive public discussion, has undergone many changes and should become shorter (now up to four years) and less expensive.

The new law introduces a new precondition for the insolvency process – during the last six months the private individual concerned must have been a taxpayer in Latvia. The administrator and creditors – who previously had little chance to influence insolvency processes – have been given larger rights. Additionally, creditors can dismiss the administrator.

France

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Substantive consolidation towards an Italian company?

In France, the issue of substantive consolidation of an insolvency proceeding does not entail any problem as long as the judicial order applies to a company registered in France. In fact, the French commercial code authorises the courts to consolidate the assets of two or more corporations (or any other legal entity) in several cases: if assets and liabilities are mixed, in case of fraud, or if the company is fictitious and shows an artificial fragmentation of entities. The order called "extension of the procedure" under French law (C. com., Art. L. 621-2) is often applied by commercial courts in order to repair artificial separations of legal persons and grant to creditors a better payment.

In a comparative way, the legal conditions for extension are quite similar to those adopted in the UNCITRAL Guide on corporate groups. However, difficulties arise when the target company has its registered office located abroad.

In this case, the French Court of appeal (*Aix-en-Provence*) had decided to extend a French insolvency proceeding opened in respect of a French group of companies from which the Italian company was belonging to. The Court of Appeal gave its decision with regard to the intermingled financial relations between those two companies.

However, the French Supreme Court (*Cour de Cassation*) has decided to file preliminary questions with the Court of Justice in Luxembourg. These two questions are of a great practical interest.

The *Cour de cassation* was wondering whether ordering a substantive consolidation could be viewed or not as a judgment opening an insolvency proceeding? The question addressed to the European Court of Justice is whether an order of consolidation could be considered equivalent to an order opening insolvency proceedings regarding their similar effects?

In the case of a positive answer another question arises: is such a decision contrary to international jurisdiction provided for by the EU Regulation? Could the French court consider that the COMI of the foreign company is in the same place as the French company, because of the confusion of their estates and liabilities?

The author is of the opinion that two responses are then possible. In favour of a positive answer, it may be argued that it is possible to consolidate the assets of the French and the foreign corporations and to consider the effectiveness of EU regulation. It implies that full effect to the main proceedings should be given avoiding the risk of fraud, which is often the case in confusion of estates and liabilities.

In favour of a negative answer, one should consider that the local law cannot ignore the rules of international jurisdiction established by the EU Regulation for a foreign company. Therefore, we are waiting with great interest the decision considering that in any case, COMI should not be located in the jurisdiction of the French company on the sole basis of "confusion". The author is of the opinion that reasons for consolidation are apart from the criterion of the COMI as defined by the EU Regulation (Recital 13) and by ECJ in its *Eurofood* decision.

To conclude, we could add a third question: could a decision of a local court ordering substantive consolidation against a foreign company be contrary to public policy in the foreign State? The answer does not depend on the EU regulation but on the foreign law. Public policy would not be threatened if the foreign law has provided for a similar mechanism. This is the case in Italy...

Spain

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Company abandonment in Spain – Update

Since drafting an article for the Autumn 2010 edition of eurofenix, namely "Company abandonment in Spain: Impact on the system of managerial liability" (pages 36-37) there has been a change to the law governing companies. The new law: *The Real Decreto Legislativo 1/2010 de 2 de Julio por el que se aprueba el texto refundido de la lay de Sociedades de Capital* (The Royal Decree Legislation of the 2nd June 2010 which reforms the law of capital companies) came into force in Spain on 1 September 2010 (save for article 515 which will not come into force until the 1st July 2011).

While the aforementioned law is in theory a new law, it is in practice a reworking of the older laws which it replaces; namely the *Ley de Sociedades Anónimas of 1951* (The Law of Stock Companies, referred as LSA) and the *la Ley de Sociedades de Responsabilidad Limitado of 1953* (The law of Limited Liability Companies, referred as LSRL). The intention of the legislature is clear in that by introducing this reformed law they wished to consolidate and clarify a number of older pieces of legislation in one straightforward text. Furthermore, it removes the differentiation between various types of companies in the Civil Code and brings all capital companies under the auspice of one piece of legislation.

What the new law attempts to do therefore, is to modify and clarify the older laws to present a more simplified and accessible version of the current laws in place. As such there are no significant amendments to the legal context of the law. The main changes are to the numbering of the articles and to its presentation.

In the aforementioned eurofenix article, reference was made to various articles including articles 260–263 of the LSA, articles 104 and 105 of the LSRL and articles 133 and 135 of the LSA. The impact of these articles and the consequences for the directors was dealt with in the Autumn edition article and I do not intend to repeat the content in this article. Suffice to say that that the new law continues to apply, in principle, the same obligations and liability to directors, especially in those aspects included in the aforementioned article. Changes therefore relate to slight modifications, renumbering of the articles and its presentation. The details in relation to the above mentioned responsibility and liability can now be referenced under articles 364-367 of the LSC (Ley de Sociedades de Capital/Law of Capital Companies).

As such the content of the Autumn article and the legal requirements laid out therein continues to be relevant and pertinent except with reference to the numbering of the articles.