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Czech Republic:
The 2017 Amendment to the Insolvency Act and its possible effects on statistics

As has been pointed out in previous issues of Eurofenix, an extensive amendment to the Insolvency Act took effect on 1 July 2017 (2017 Amendment).

The 2017 Amendment brought several substantial changes to a number of aspects pertaining to insolvency proceedings, including most notably the security of future or contingent claims (e.g. bank guarantees), the assessment of a company's insolvency and its discharge from debts. Looking at the statistics concerning insolvency proceedings in 2017 and comparing them with the data from 2016* one might make a couple of remarks regarding the 2017 Amendment.

Number of insolvency petitions

From 2013 to 2016, the number of insolvency petitions gradually diminished at a rate of about 8% annually on a year-to-year basis. Whereas in 2013 37,613 insolvency petitions were filed, in 2016 only 29,493 were submitted. In 2017, however, the fall was steeper as only 23,135 petitions were registered with insolvency courts.

Types of insolvency proceedings

Under the Czech Insolvency Act, three basic methods for resolving a debtor's insolvency exist: liquidation (*konkurs*), reorganisation and discharge of debts (*oddlužení*). As in 2016, the discharge from debts accounted for almost 90% of all insolvency proceedings in 2017.

Creditors' insolvency petitions

The data reveals that the decrease in the number of petitions concerns both creditors' as well as debtors' insolvency petitions. As regards creditors' insolvency petitions, readers might be reminded that the 2017 Amendment *inter alia* did touch upon the position of creditors by making the preconditions for submitting insolvency petitions stricter, particularly with respect to ascertaining the creditors' claims.

Debtors' insolvency petitions

As mentioned above, most of the insolvency proceedings are of the type of discharge from debts, whereas only a minority of them are initiated on the basis of the creditor's insolvency petition. Therefore, the fall in the number of debtors' insolvency petitions is presumably attributable to changes related to the discharge from debts proceedings as the most "popular" type of insolvency proceedings.

The 2017 Amendment stipulates that debtors themselves are in principle no longer eligible to file a motion for discharge from debts, they must be assisted by legal professionals (mainly attorneys or authorised entities). Moreover, the fees for the preparation of motions for discharge from debts are subject to regulation. This legislative move is targeted against dubious legal entities which in many instances would charge disgracefully large fees. Nevertheless, anecdotal experience suggests that nowadays only a limited number of legal professionals are willing to assist debtors, because the authorised entities are overloaded with too many debtors' cases to treat.

Against this background, it is not surprising that the statistics show a sharp fall in the number of proceedings dealing with the discharge from debts. In 2016, insolvency courts dealt with 26,596 motions for discharge from debts, with confirmations in 22,084 proceedings. In 2017, the influx of new proceedings for the discharge from debts sharply decreased to 21,007 cases, and only 18,428 confirmations were issued.

The ratio between discharge from debts in the form of a sale of a debtor's assets and that of a repayment plan stayed more or less the same. Less than 3% of all cases were solved in the former way, whereas more than 97% were in the latter. ■

**As concerns the data, the author refers to statistics provided by the Ministry of Justice of the Czech Republic, based on the request submitted pursuant to the Freedom of Information Act.*

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US Chapter 15:
Delaware court sends U.S. creditor packing… to Italy

In the Chapter 15 proceedings of Energy Coal S.p.A., the Delaware Bankruptcy Court required a U.S. creditor to recover its claim in Italy.

Because there is no uniform global insolvency law, and every country has its own insolvency law, The United Nations Commission on International Trade Law (UNCITRAL) developed the UNCITRAL Model Law on Cross-Border Insolvency (1997) to facilitate cooperation and uniform outcome in cross-border insolvencies. 43 countries have adopted the model law, and the U.S. version is Chapter 15, which is similar to the "foreign main" proceedings in Italy. Founded on principles of comity, the U.S. courts assist the foreign insolvency court in cross-border insolvencies. A key benefit of Chapter 15 to foreign debtors is the use of the "automatic stay" which enjoins creditor action against U.S. assets. Another important benefit is the foreign debtor's ability to obtain discovery and assert claims against U.S. companies.

MacEachern Energy LLC ("U.S. Vendor") was a vendor owed at the level of 2.2 million euros by Energy Coal S.p.A. ("Energy Coal"), an Italian company doing business in the U.S. U.S. Vendor also owed money to Energy Coal, creating a right of set off of mutual debts. In April, 2015, Energy Coal filed for insolvency protection in Italy, under the Italian Insolvency Law, the Concordato Preventivo. In October, 2015, Energy Coal also filed for Chapter 15 proceedings in the U.S. in order to obtain the U.S. "automatic stay", aiming to forbid

U.S. creditors to pursue its U.S. assets.

In the Italian proceedings, Energy Coal submitted a restructuring plan for approval by the court in September, 2016. The Italian plan provided that unsecured creditors would receive 7% or less as a dividend. In the Chapter 15 case, Energy Coal moved to have its Italian plan enforced in the U.S., by order of the Delaware Bankruptcy Court. Specifically, the claims of U.S. creditors were subject to the Italian plan, and creditors were enjoined from seeking judgments in the U.S.

U.S. Vendor objected to the Italian plan, particularly against the injunction preventing it from recovering 100% from Energy Coal in the U.S. and the effective elimination of its set off rights. Energy Coal could recover 100% of its claims from U.S. Vendor, while U.S. Vendor would have received 7% or less on its claims. In support of its objection, U.S. Vendor cited its contract with Energy Coal, which provided for the Florida law and venue to be applied to any contract disputes.

In light of U.S. Vendor's objection, Energy Coal agreed that U.S. Vendor could reduce its claims to a judgment in Florida courts. However, Energy Coal's position remained that any judgment would be subject to the Italian plan and could only be paid pursuant to the Italian proceedings, meaning that U.S. Vendor must litigate in Italy.

The Delaware Bankruptcy Court ruled that comity and the need for cooperation and assistance in cross-border insolvencies outweighed the parties' contractual choice of law and choice of forum provisions. U.S. Vendor was thus left to litigate in Italy regarding the enforcement of its judgment and distribution on its claim. A piece of good news for U.S. Vendor is that the Delaware Court acknowledged the loss of U.S. Vendor's set off rights and hinted that if Energy Coal sought recovery of claims owed by U.S. Vendor, the Court would allow U.S. Vendor to assert set off of its entire claim as a defense. ■

> **THE U.S. COURTS ASSIST THE FOREIGN INSOLVENCY COURT IN CROSS-BORDER INSOLVENCIES**

Italy:
NPL and insolvency proceedings

Recently, the attention of the financial–economic world has focused on non-performance loans, (hereafter NPL).

The term "NPL" stands for bank loans emerging from mortgages, loans and funding, difficult to recover due to a worsening of the economic and financial situation of the debtor, no longer able to perform all or part of his/her contractual obligations.

Within the macro-category of the NPL, the Bank of Italy, in application of the EU Regulation 227/2015, has foreseen a new and precise classification of the NPL, in particular:

- Non-performing loans that are the debt exposures of subjects in an insolvency situation or situations alike. In this case, it is not necessary that the status of "non-solvency" be judicially established;
- Probable defaults or exposures - other than those classified as non-performing - for which the Bank, without recourse to actions such as the enforcement of guarantees, evaluates unlikely that the debtor regularly performs his/her obligations;
- Expired past due and/or overdrawn exposures or exhibitions that have expired or exceed the credit limits for more than 90 days and are above a materiality threshold.

The issue related to NPLs suffered by the Italian banks is largely the result of the recession that hit the Italian economy in recent years and especially the long time needed for the judicial recovery of the credit.

In the context of non-performance loans, procedures aimed at recovering the repayment of those loans play a fundamental role . On the one hand, there are the procedures regulated by the Civil Code - which have to be excluded from this brief analysis – and on the other, the insolvency procedures.

With regard to the latter, unfortunately, their duration is too long; in fact, the information provided by the Bank of Italy shows that recovery takes place within approximately the first five years.

The element of slowness of recovery characterises not only the "liquidation" procedures such as bankruptcy and the composition with creditors which have a liquidation purpose, but also the restructuring procedures provided in the Italian law.

In fact, in most cases, these proceedings are still ongoing four years after they commenced.

Furthermore, it is useful to consider the restructuring procedures that are transformed into liquidation procedures.

With regard to individual recovery procedures, the composition with creditors deserves a particular attention. In fact, despite several amendments to insolvency law aimed at pointing out the restructuring purpose[2], these proceedings are still being used nowadays for liquidation purposes. It is important to highlight, however, that according to the analysis conducted by the Bank of Italy, the number of recoveries obtained through the composition with creditors is higher than those obtained through other procedures.

In this context, in order to avoid that the presence of non-performance loans in the balance sheet, adversely affecting the granting of credit, the recent reforms related to the bankruptcy law will hopefully reduce the time needed for the recovery and increase the positive outcome of insolvency proceedings.

At the European level, however, one should be aware of the directives of the EBA (European Banking Authority) aimed at reducing non-performing loans by exhorting the operational and governance bases for effective recovery, which shall be implemented by January 2019. ■

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