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Changes ushered in by the reform of the Revised Spanish Insolvency Law

Legal Alert

September 2022

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6 September 2022 saw the publication in the Official State Gazette of the **reform of the Revised Insolvency Law**, which seeks, inter alia, to transpose the European restructuring and insolvency Directive [Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019], in order to provide viable companies facing financial difficulties with early restructuring frameworks that enable them to overcome such temporary situations.

The above reform, which was necessary to transpose the aforementioned Directive into Spanish domestic legislation by the 17 July 2022 deadline, following a one-year extension period, was finally published in the Official State Gazette on 6 September 2022 and will enter into force 20 days following publication, with the exception of the book setting out the special procedure for micro enterprises and the provisions pertaining to deferrals or instalment payments of tax debts granted by the State Tax Agency, which are generally set to enter into force on 1 January 2023.

Only four of the 252 amendments proposed by the Upper House and submitted to a vote in the extraordinary plenary session held on 20 July prevailed, contrary to widespread predictions. They were nevertheless ultimately rejected when the Law was returned to the Lower House.

The main new developments brought in by the reform, which have sparked further debate in recent months, are as follows:

1. Notification of the commencement of negotiations with creditors: likelihood of insolvency and stay of enforcement of group collateral

One of the main changes introduced by the reform is the incorporation into Spanish law of the concept of **likelihood of insolvency**, which permits debtors to make use of pre-insolvency mechanisms early and avail themselves of the protection afforded by notification of pre-insolvency when they do not expect to be able to regularly meet their obligations falling due in the next **two years**.

The three-month period in which debtors can negotiate a Restructuring Plan with their creditors may be extended by a further three months under certain conditions.

Requests for the **stay or prohibition of the commencement of individual enforcement actions or collateral enforcement** during negotiations with creditors may now be extended to in rem guarantees and collateral granted **by group companies**, where the enforcement of such collateral jeopardises the viability of such companies.

Also, the legislation now includes a detailed list of the content and subjective and objective requirements governing all notifications of the commencement of negotiations with creditors.

The provision whereby individual enforcement actions affecting public claims will not be stayed remains in place. Similarly, the requirement whereby debtors must wait for one year before they can once again make use of this safeguard mechanism during negotiations with creditors continues to apply.

2. Restructuring plans

The Reformed Law unifies existing pre-insolvency tools under the new concept of Restructuring Plans, the content of which has been broadened considerably to permit any modification of the debtor's assets or liabilities, as well as operating or corporate restructuring and even the total or partial transfer of assets.

The range of claims that may be affected by these Restructuring Plans has increased significantly with respect to the previous scenario, where refinancing arrangements only affected financial liabilities. Although such Plans may now include public claims, in order for this to happen, debtors must demonstrate that they are up to date with the relevant payments and that the relevant claim is less than two years old. Moreover, such claims may only be deferred for up to 12 months.

The Reformed Law groups creditors into classes, whereby creditors holding the same rank in the order of payment of claims must belong to the same class. Sub-classes based on objective criteria and common interests are also permitted.

It is provided that creditors holding claims affected by Restructuring Plans must vote together by class, the general rule of thumb being that a majority of the classes must vote in favour of the Plan before it is approved, albeit with a number of exceptions.

Court approval of these Restructuring Plans will enable, as the case may be, their effects to be extrapolated or extended within and between classes ("cramdown" and "cross-class cramdown"), and will also permit the termination of contracts and the protection of new or interim financing.

The Reformed Law introduces the figure of expert in the field of restructuring who, in certain cases, may be appointed by the court and who will assist the debtor and/or the creditors in negotiating and drawing up the Plan.

3. Sales of production units: continuity, publication, appointment of an independent expert and jurisdiction of the insolvency court

The new wording of the Law includes an additional safeguard in respect of the sale and purchase of production units by providing that the offeror must undertake to continue the business activities for at least two years. Breach of this duty will entitle any affected parties to claim compensation for damage and loss from the acquirer.

Moreover, to incentivise this divestiture mechanism, the debtor may ask the court to appoint an independent expert to solicit tenders for the acquisition of the production unit. All tenders must be appropriately published on the Public Insolvency Registry's divestitures site.

Under the new legislation, the offer to purchase the production unit may be made by the debtor's workers duly established as a cooperative, a worker-owned entity or investee, and parties interested in business succession. Furthermore, the lawmaker has made sure to prioritise this group in the awarding process in the event that tenders for identical amounts are received.

The new wording of the Law also consolidates the jurisdiction of the commercial courts to define the scope of the assets and liabilities transferred in production unit sales, affording them exclusive and exclusionary competence to declare the existence of business succession, thus drawing a line under a heated debate on this subject.

4. Duration of the insolvency proceedings and fast-tracking

The Reformed Law provides for certain instruments aimed at reducing the duration and streamlining the effectiveness of insolvency proceedings. Of note in this connection is the 12-month cap on the duration of insolvency proceedings (although the court may order an extension of that time period on an exceptional basis or in view of the complexity of the case) and the preferential processing of appeals lodged in insolvency proceedings.

Mechanisms for subjecting collection of the insolvency managers' fees to the duration of the insolvency proceedings have also been introduced and, accordingly, the common phase and the arrangement phase should be limited to six months, while the liquidation phase should be limited to eight months. Exceeding these time limits could bring about a reduction in the aforementioned fees.

5. Discharge of unpaid liabilities: priority of public claims

The Reformed Law refers to the Discharge of Unpaid Liabilities (EPI, for its Spanish acronym), equivalent to the Credit for the Discharge of Unpaid Liabilities (BEPI, for its Spanish acronym) provided for in the original Law.

After some debate, the limit on the amount of public claims eligible for discharge has been set at €10,000, including amounts owed to both the public treasury and social security. It should also be noted that these public claims will only be eligible for discharge in respect of the debtor's first EPI application.

6. Arrangement with creditors: Detailed regulation

The effectiveness of the arrangement phase has been somewhat limited over recent years. With this in mind, the lawmaker has sought to better organise and define the content of proposed arrangements. Two new developments are particularly worth noting in this connection. Firstly, the possibility of the debtor implementing orderly structural changes and, secondly, in line with the protection now afforded to public claims, the prohibition on implementing reductions or deferrals in respect of social security claims.

Elsewhere, and after a good deal of debate, claims assumed by the debtor during the period for performing the arrangement (formerly classed as post-insolvency order claims) are now classed as insolvency claims.

7. Special procedure for micro enterprises

One of the most significant developments in the Reformed Law is the creation of a special procedure for processing what have been known until now as insolvency proceedings, in the case of micro enterprises. In an attempt to expedite the procedure, the process is to be simplified and the procedural deadlines shortened, by providing debtors with standard forms.

Lastly, this means of processing will only be available to debtors engaging in a business or professional activity that has employed fewer than 10 workers on average over the preceding year and with annual revenues of less than €700,000 or liabilities of less than €350,000, based on the last annual accounts closed in the year preceding the application.

Debtors must now appoint both legal counsel and a court procedural representative and, in the absence of an obligation to appoint an insolvency manager, the role of both of the above, and of the Counsel for the Administration of Justice, is of particular relevance.

Under this new procedure and in line with the solutions traditionally available in the insolvency proceeding, the regulations provide that the special procedure for micro enterprises may lead to either a continuation procedure, whereby the business activity will continue, or a liquidation procedure, where continuation of the activity is not possible or where so requested.

Finally, it is worth noting that, per the transitional provisions, save for certain exceptions, insolvency proceedings commencing prior to the entry into force of the Reformed Law shall be governed by the former legislation.

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