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# Nordic-Baltic Recommendations on Insolvency Law

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Drafted by the  
Nordic-Baltic Insolvency Network





# Nordic-Baltic Insolvency Network

## *Preface*

The Nordic-Baltic Insolvency Network was established by a Swedish initiative in November 2010. The main reason for this initiative was the financial crisis that the Baltic States had endured, revealing the fact that there were considerable differences not only between these countries' insolvency systems, but also between the Baltic systems and those systems in the Nordic countries. The initial issue was whether this diversity was justifiable and appropriate, as it was assessed that these divergences would have a negative effect on willingness to invest in this part of Europe.

The main purpose of the Network has been to encourage efforts towards the substantive harmonisation of insolvency law. This area has been greatly discussed of late and to some extent even explored. However, this has not resulted in any specific legislation, which is disappointing in many respects.

The thought behind this network is to strengthen the Nordic and Baltic States' participation and influence within such a process for the purpose of arriving at the first stage of developing common principles, which are suitable and much needed, in key areas where substantial legal differences can be found to exist.

The productivity of the Network is owed to a number of academics and expert practitioners from Sweden, Norway, Denmark, Finland, Estonia, Latvia and Lithuania who have regularly met to discuss common texts containing recommendations for various blocks of subjects. These texts have then been gradually worked through resulting in the recommendations now presented in their final version that has been mainly prepared by Professor Mikael Möller at Uppsala University.

The emphasis of the Network is on reorganisation law, as the acts that have developed in the last 25 years in this area have hardly had any consideration for the regulations of neighbouring countries. In light of the interaction between the regulations for liquidation and reorganisation, we have also discussed and developed recommendations on important liquidation issues in a similar way as with, for example, UNCITRAL's Legislative Guide on Insolvency Law.

Each national group of the network consists of an average of 5–7 people. The Chairman of the Network and contact person for the Swedish group is Lawyer Erik Selander, and the other contacts for the various national groups are: Lawyer Siv Sandvik (Norway), Professor and Lawyer Anders Ørgaard (Denmark), Lawyer Pekka Jaatinen (Finland), Lawyer and Professor Paul Varul (Estonia), Lawyer Gatis Flinters (Latvia) and Professor and President of the Supreme Court Rimvydas Norkus (Lithuania).

Erik Selander  
*Chairman*



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## **Overall objectives and features of an effective and efficient insolvency law**

- The general objective of insolvency law is to maximize efficiency of the economy by facilitating trade and supporting an effective credit system and a favorable investment climate.
- Insolvency law shall provide a transparent, predictable and cost-effective set of rules that allows, based on the circumstances of the individual case, the preservation and maximising of the value of the debtor's assets by enabling, on the one hand, reorganisation of viable businesses and, on the other hand, rapid liquidation of businesses that have no prospect of survival.
- A reorganisation should never be an end in itself, but is to be carried out in those cases where an ongoing business has a surplus value which is effectively greater when the necessary components of the business are held together instead of being broken up and sold off in fragments. In light of the aforesaid, the creditors should not involuntarily receive less than in a liquidation. Generally, the option that maximises asset values is also the best option for society on the whole and other stakeholders.
- Insolvency law should be governed by the principle of equal treatment of creditors.
- Insolvency law should also be neutral in the sense that it does not create incentives for the debtor or a particular group of creditors for their own part to choose liquidation over reorganisation, and vice versa. The choice between the proceedings should, in other words, be governed by the overall objectives of insolvency law and not special interests. The interest of the general body of creditors should always prevail.
- Insolvency rules should create incentives for the owners and management of the debtor to seek a comprehensive settlement with the creditors at such a time that the value of the assets has not been eroded to such an extent that an unfavorable liquidation is inevitable.
- Insolvency law should provide national and international investors and lenders predictable and adequate protection for established security interests. This includes the value of the securities is not eroded without compensation during the insolvency proceedings and that a predictable order of priority are established.
- Insolvency law is to provide rules which enable efficient and effective management of insolvency proceedings concerning groups of companies.

## **I. Application and commencement of insolvency proceedings**

### **Who should have the right to initiate the commencement of proceedings?**

#### *Liquidation*

1. Both the debtor and a creditor shall have the right to apply for, and to have the debtor put into liquidation.

#### *Reorganisation*

2. The debtor is to have the right to apply for and to obtain the commencement of a reorganisation.

3. As a general rule the debtor's application or consent should also be required in order to commence a reorganisation. A creditor can be given the right to apply, but should thus not have the right to initiate the court commencing proceedings against the debtor's wishes.

4. On certain conditions a reorganisation could, however, be commenced without the debtor's consent. These conditions should be that:

- (a) commencement is based on the debtor's insolvency,
- (b) the debtor is divested or could be divested of the right of disposition, either if this right is taken over by the administrator or by the reorganisation being terminated by way of a conversion to liquidation, and
- (c) there are to be provisions that facilitate, or create good opportunities, to achieve the management or ownership changes that are necessary in order for the business to be continued with sustainable profitability.

### **The choice and relationship between liquidation and reorganisation**

5. The proceedings should be initiated from the start as either a liquidation or a reorganisation and should not start with a neutral investigative phase. The application is to include a specific claim that either one or the other of the proceedings should be commenced.

6. When the debtor has applied for reorganisation and the application is not granted the court should not have the right to decide on liquidation as an alternative.

7. A reorganisation that has been commenced may, however, in the course of the proceedings be converted into liquidation. This would require that the debtor is distrusted or misusing the reorganisation proceedings, the creditors' rights are at risk, there is no prospect of implementing a reorganisation plan or the reorganisation should not be continued for some other good reason. The reorganisation should, however, not be converted into liquidation if the debtor opposes this and can prove that he is solvent.

If it is sufficient that the debtor is divested of the right of disposition, a less restrictive and supplementary solution may be that the reorganisation continues under the direction of the administrator.

8. An application for reorganisation should be considered before a copending application for liquidation, irrespective of who made the application.

### **Grounds for commencing proceedings and their review**

#### *Liquidation*

9. A liquidation may be commenced when the debtor is *insolvent*. This means that he is unable to pay his debts as they become due, provided that the inability is not merely temporary. Insolvency in this sense should be the single commencement standard.

10. When the application is submitted by the debtor, his statement of insolvency should be accepted provided that there are no special reasons for questioning the statement.

11. When the application is made by a creditor and the debtor does not accept it, the creditor, in principle, should be required to substantiate that the debtor is insolvent.

However, insolvency should be presumed when

(a) the debtor, despite the request by the creditor, has failed to pay a clear and due debt within a short additional period of time, the creditor after that period has applied for the debtor to be put into liquidation and the debt has still not been paid at that stage,

(b) if an attachment within a certain number of months before the application has revealed that the debtor had no assets to cover full payment of the executed claim, or

(c) the debtor by way of a declaration addressed to a wider circle of creditors has announced that he suspends payments.

Notwithstanding the provisions of the first and second paragraph, a creditor should not be entitled to have the debtor put into liquidation if adequate security is set for the creditor's claim or, if the claim is not yet due for payment, such security is offered by a third party.

#### *Reorganisation*

12. In order for a reorganisation to be commenced a material requirement is that the debtor on the one hand has financial problems as described in section I:13, on the other hand is able to be reorganised as described in section I:14.

A reorganisation should not be commenced and should be set aside if it is likely that the debtor will not be able to pay all post-commencement claims.

13. From a financial perspective a reorganisation may be commenced when the debtor has temporary liquidity problems, or in the event such problems are expected to arise in the short-term, but also when he is insolvent in the sense described in section I:9. When the proceedings on a creditor's application can be commenced without the consent of the debtor, insolvency should be the single financial commencement standard.

When the proceedings are commenced after the application or the consent of the debtor, the debtor's statement about his financial problems should be accepted in a similar manner as in the case of liquidation, unless there are special circumstances.

When the proceedings are commenced after an application by a creditor, the same rules for insolvency should apply as in the case of liquidation according to sections I:9 and 11 above.

14. The requirement regarding the debtor's ability to become reorganised should mean that the applicant must make it probable that a reorganisation can be carried out in compliance with applicable rules. This requirement should be subject to a real case review regardless of how the proceedings have been initiated. The review should primarily be based on a preliminary reorganisation plan which should be included in or accompany the application. The content of this requirement is thus primarily dependent on which requirements should be imposed on the preliminary plan according to section I:16 below.

15. The creditors should be afforded the opportunity, and the administrator should be obligated, to participate in a meeting before the court a few weeks after the commencement decision for the purpose of considering whether or not the reorganisation should continue and, if the law permits and if it has not already been done, whether the right of disposition should in such cases be taken over by the administrator or remain with the debtor. The creditors' position should not be manifested by way of a formal vote but by expressing their opinion, which along with the administrator's, will be taken into consideration by the court.

#### **The reorganisation application's content and support**

16. An application for reorganisation should include a preliminary reorganisation plan. The law must identify which fundamental elements *should* be included in this plan and in addition what it *could* include with regard to reorganisation measures that would otherwise be contrary to other legislation. The preliminary plan should indicate the legal and actual measures that are considered necessary to carry out during and after the proceedings in order to resolve the difficulties of the debtor or the business, and which are required in order for the business or parts thereof to continue with sustainable profitability by the debtor or someone else.

17. In addition to the preliminary reorganisation plan in the strict sense, the application should include certain descriptive and explanatory elements, such as information about known creditors, debts and assets including securities held and their value, the latest annual reports, a description of the debtor's business, the reasons for the difficulties that have arisen and the estimated outcome of an alternative liquidation.

All information provided in the application and the preliminary plan should become public after the commencement of the proceedings. Any information about the debtor company's production methods, marketing strategies and the like could, however, be kept secret under provisions of confidentiality, as the company may incur substantial damage should such information be revealed.

18. Notwithstanding that the major creditors' trust is normally essential for a successful reorganisation with the debtor at the helm, a formal requirement that the application or the preliminary plan must be supported by certain creditors or a certain portion of the creditors should not be imposed.

Neither should it be required that the application has been communicated to the creditors before being submitted, nor should there be any communication about the application by the court before the commencement decision has been made. In this regard, the early creditors' meeting described in section I:15 should be sufficient in order to satisfy the interest of the creditors' influence and will provide the court with information as to what degree the debtor and the reorganisation has creditors' support.

### **Information regarding insolvency proceedings**

19. The court's decision regarding commencement of the insolvency proceedings should be made public in a national/international insolvency directory.

20. The liquidation trustee or the reorganisation administrator should be obligated to send a notice regarding the proceedings to all known creditors without undue delay from the commencement of the proceedings. This notification is to include instructions about the procedure for submitting of claims, various time limits during the proceedings that ought to be observed and the consequences of non-compliance with those time limits.

Notifications under the first paragraph need not be sent if the number of creditors is very large. Information on these aspects should instead be available on a website.

21. Within a certain time from the commencement of liquidation proceedings, the trustee is to be required to send an inventory of the liquidation estate to the court. This inventory should contain detailed information regarding the debtor's assets and debts as well as contact information to all known creditors.

Regarding reorganisation there are similar provisions, related to the requirements for preliminary and final reorganisation plans, in sections I:17 and XII:6.

## **II. Representatives' liability due to the continued operation of insolvent companies**

### **Background**

1. Insolvency law regulations on personal liability related to the continued operation of companies in distress should exist in order to help ensure that reorganisations and creditor settlements take place at an early stage. The regulations should be aimed at the management of the company, primarily the board of directors in limited companies, which is normally exclusively qualified to initiate insolvency proceedings on behalf of the company. Management liability could also contribute to boards of insolvent companies become more inclined to prioritise the creditors' rather than the owners' interests.

2. In many countries there is criminal law, tort law, tax law or company law regulations which under similar conditions as recommended here can lead to representatives' liability. Even if these regulations are often difficult to apply and exist to fulfil other purposes, they can to a certain degree interact with the insolvency law regulations. The network does not address the question whether the recommended insolvency law rules exclusively should regulate financial liability in cases of continued operations of companies in distress, or whether they should work in parallel with other rules. The network has neither taken into consideration to what extent rules in other areas of the law need to be amended.

### **The proposed rules**

3. If a company's business has improperly been continued after the company became insolvent, and a representative of the company knew or should have known about the insolvency and the circumstances that made the continued operation improper, the representative shall be required to pay compensation to the company's insolvency estate corresponding to the total disadvantage incurred by the estate due to the improper continued operation.

The recommended legal effect means that all creditors in the insolvency proceedings in priority order will share the compensation for the loss which the continued operations have caused the estate compared with the outcome of a hypothetical insolvency proceeding on the first day of the liability period.

An individual creditor should not be entitled to compensation from the representative for a loss that is covered by a claim made for the benefit of the estate.

4. An action on behalf of the estate may be brought by the person or persons who are entitled to make a claim for recovery to the estate. Furthermore, the recovery law regulations should apply with regard to the manner and timing of the action. In this set of recommendations, these issues are regulated in sections VI:13-17 below.

### **III. Immediate legal effects of the commencement decision**

#### **Restrictions on the debtor's right of disposition**

##### *Liquidation*

1. At the commencement of a liquidation the debtor should be denied the right to dispose over assets and manage the business ("*the right of disposition*") to the extent that corresponds to the liquidation estate's right to seize the debtor's property. Additionally, the debtor should not be permitted to incur new obligations that may be claimed in the liquidation.

Legal actions undertaken by the debtor contrary to the first paragraph should have no effect in the liquidation. Counterparties, who in good faith have entered into legal transactions with the debtor should, however, to a certain extent be protected through special exemption rules.

##### *Reorganisation*

2. When a reorganisation is commenced at the request of the debtor, the debtor should as a starting point maintain the right of disposition. The debtor should, however, not be allowed to pay debts or fulfil other obligations which occurred prior to the reorganisation, nor provide security for such obligations, without the consent of the administrator. Nor should the debtor without consent be able otherwise to dispose over assets or incur new obligations outside the ordinary course of business.

Legal actions undertaken by the debtor without the required consent should have no effect, unless the counterparty was in good faith concerning the debtor's lack of entitlement.

3. When a reorganisation is commenced at the request of a creditor, without the consent of the debtor, the debtor should be denied or, at the request of a creditor or the administrator, may be denied the right of disposition to such an extent as provided in the event of liquidation.

#### **Asset seizure through a liquidation estate**

4. At the commencement of a liquidation, the debtor's assets, to the extent they may be transferred or by other means be converted into money, are seized by a liquidation estate ("*the estate*") that is represented and managed by one or more trustees.

For the description and formulation of different liquidation rules there are practical and educational advantages to considering the estate as a special legal entity separated from the debtor. The same result may, however, be achieved by using a different legal technique. Likewise, it should not make any factual difference if the estate is considered as taking over the debtor's assets with ownership or with special management and sales rights, instead real arguments and not formal labeling may determine the content of the specific rules.



## **Protection of the estate against enforcement and sale of securities**

### *Liquidation*

5. After the commencement of a liquidation the assets that are included in the property seizure cannot be attached or subject to other enforcement for claims against the debtor.

There should be an exemption from the first paragraph for claims assisted by a security interest in specific property.

6. If a secured creditor, as referred to in section III:5 paragraph 2, requests that his security should be sold and his entitlement to payment is undisputed or established through a legally binding decision, a sale of the security should not be postponed.

The sale should, however, be postponed if it is necessary to avoid that the estate incurs considerable loss or a possible restructuring solution is significantly hindered.

### *Reorganisation*

7. Once a reorganisation has been commenced, attachment and other enforcements should not be allowed for claims which have arisen prior to the reorganisation.

An exemption from the first paragraph should be made for claims assisted by a security interest in property which is not at the debtor's disposal.

At the request of a creditor exemptions from the first paragraph may also be made for property which is clearly not needed for the debtor's business.

8. During the reorganisation the debtor may not be put into liquidation for claims which have arisen prior to the reorganisation, unless there are special reasons to assume that the creditor's rights are seriously at risk or a specified legal reason exists for terminating the reorganisation.

## **Protection of security values**

9. A creditor holding a security interest in specific property, should be entitled to compensation for any decrease in value of the property that is due to it having been used for continued operations pursuant to sections III:6 or 7. The payment of compensation should always be settled against the secured capital debt.

10. If a security, as referred to in the preceding section, can be sold regardless of insolvency proceedings, it should be used only to cover costs relating to the care and sale of the security.

What in this Chapter has been said about securities also applies to their returns.

## **IV. Treatment of the debtor's contracts**

### **General scope of the rules**

1. Insolvency law is to provide rules on the treatment of current contracts under which the debtor and its counterparty at commencement of the proceedings have not yet fully performed their obligations (*"the debtor's contracts"*).

### **The insolvent side's right to choose between continuation and rejection**

2. The rules regarding the debtor's contracts should be based on the insolvent side having the right to choose whether to continue a contract or reject it.

In case of liquidation, *"the insolvent side"* refers to the liquidation estate, represented by the trustee.

In a reorganisation, *"the insolvent side"* refers to the debtor, whose right to choose under the first paragraph should be exercised with the consent of the administrator. In reorganisations where the debtor's right of disposition is taken over by the administrator, the right to choose should be exercised by the latter.

3. The liquidation estate's right to choose between continuation and rejection under section IV:2 should also apply to contracts that have been subject to a continuation decision in a previous reorganisation that has been converted to the current liquidation.

### **The counterparty's right to request a decision**

4. The counterparty may request that the insolvent side provides notice within a reasonable time frame as to whether it will continue or reject the contract.

### **General effects of the continuation decision**

5. The insolvent side's choice to continue the contract should mean that the counterparty shall fulfil its remaining performances under the contract and that the insolvent side shall provide consideration accordingly.

To the extent the debtor's performances under the contract cannot be divided without significant inconvenience to the counterparty, the insolvent side shall also issue consideration for such performances the counterparty may have fulfilled before the proceedings.

To the extent that the counterparty's claims under the contract are covered by the continuation decision, they should be treated as post-commencement claims (see Chapter X below). The same applies to those claims that the insolvent side may require the counterparty to honour as a result of the continuation.

### **The insolvent side's right to request limited future continuation**

6. If the contract concerns continuous or divisible performances, the insolvent side should have the right to limit its continuation to a certain period or to an amount of the remainder, subject to the insolvent side providing information about any such limitation

on the continuation within a reasonable time from the notification that the contract will be continued.

What is stated in the first paragraph should not apply if a limited continuation would involve significant inconvenience for the counterparty or the counterparty has rights in rem to the debtor's performances.

### **The counterparty's right to request security**

7. If, under the contract, the counterparty is obligated to provide performance before the insolvent side has to provide consideration, and, if the counterparty's obligation to perform is due, the counterparty should have the right to request that the insolvent side provide security without undue delay.

If time has not elapsed for the counterparty's fulfilment of his remaining performance, the counterparty may request security only if there is a particular reason to protect against its losses.

### **The counterparty's right to terminate**

8. If the insolvent side does not, within the time limits specified in section IV:4 and 7, upon the counterparty's request explain that it will continue the contract or provide security, the counterparty is to be entitled to terminate the contract.

9. In a case such as referred to in section IV:3, the liquidation estate's failure should instead result in the estate being deemed to have cancelled the counterparty's remaining performances. The counterparty may then not adhere to the contract, but has the right to claim damages due to the cancellation with the same priority as other post-commencement claims from the previous reorganisation.

### **Limitations of the counterparty's contractual rights to terminate or accelerate the contract**

10. After an application to commence the proceedings has been made, a counterparty should not be entitled to terminate or accelerate the contract due to delays in payments or other performance, if the delay has occurred or is anticipated to have occurred before the commencement decision.

Nor should the counterparty be entitled to terminate or accelerate the contract with reference to the application to commencement of the proceedings, the commencement decision as such or any similar event connected to the proceedings.

11. If the contract relates to premises that the debtor uses under a rental contract, the insolvent side could be evicted due to such delay in payment referred to in the previous section only if the landlord has applied for eviction before the application to commence proceedings.

## **The insolvent side's responsibility for performances obtained and consumed after the commencement decision**

### *General rules*

12. If the insolvent side obtains a performance from a counterparty to the debtor's contract and chooses not to continue the contract, the performance should be returned.

If the insolvent side disposes of the obtained performance so that it cannot be returned essentially unchanged or undiminished, the insolvent side should be deemed to have continued the contract with regard to the obtained performance. The same should apply if the insolvent side makes use of an obtained performance that is such that it cannot be returned.

A disposal or use according to the second paragraph should not be considered to exist unless the trustee or administrator knew, or should have known, that a performance has been obtained and the contract which the performance refers to.

### *Continued use of premises*

13. If a landlord continues to make premises available under a rental contract with the debtor, the insolvent side should be deemed to have continued the contract with regard to claims for rent for use occurring later than a specified time from the commencement decision. This period should not be less than 14 days and no longer than a month.

If, in the case of liquidation, there are objects on the premises which are included in the estate, usage in accordance with the first paragraph should be deemed to exist as long as the estate has not abandoned or removed the object.

### *Continued use of labour*

14. If an employee continues to fulfil his or her obligations under an employment contract with the debtor, the insolvent side should be deemed to have continued the contract with regard to claims for compensation for work that is performed later than a specified time from the commencement decision. This period should be not less than 14 days and no longer than a month and be covered by the wage guarantee system.

## **The insolvent side's right to assign the debtor's contract**

15. The insolvent side should have the right to assign the debtor's contracts, provided that

- (a) the insolvent side has declared that the contract will be continued,
- (b) the assignee's ability to perform the assigned obligations cannot reasonably be questioned, and
- (c) the counterparty is not substantially disadvantaged by the assignment.

16. The assignment should have the effect that the assignee is substituted for the insolvent side as the contracting party. This means that the assignee shall fulfill the insolvent sides remaining contractual obligations to the extent they are covered by the continuation decision, while the counterparty shall issue consideration for the aforesaid, and that the insolvent side from the date of the assignment has no liability under the contract.

### **Deviations from the recommended rules**

17. Contract terms, which in comparison with the recommended rules regarding debtor's contracts are disadvantageous to the insolvent side, should have no effect.

18. The rules regarding the liquidation estate's right to continuation under sections IV:2 and 3, and the insolvent side's right to assign contracts under sections IV:15 and 16, should not apply to contracts whose fulfillment is essentially based on the debtor's personal efforts, or the nature of the contract otherwise indicates that the rules should not be used.

The sections mentioned in the first paragraph should not apply to employment contracts.

19. If deviations from the recommended rules on the debtor's contracts are provided in other legislation, which supersede these, the insolvency law should contain a comprehensive list of such statutory provisions.

## **V. Treatment of pending lawsuits in liquidation proceedings**

### **General scope of the rules**

1. This Chapter provides rules on the treatment of lawsuits which are pending at the time of the commencement of liquidation proceedings, regardless of whether the debtor is the claimant or the defendant. These rules should also, *mutatis mutandis*, apply to cases where a lawsuit is initiated after the commencement of the insolvency proceedings, except for the rules on information, stay of proceedings and notification under sections V:13-16 in cases where the liquidation trustee, a creditor or the debtor commences the lawsuit.

Furthermore, this Chapter initially contains some rules on judgments and arbitration awards made prior to liquidation proceedings thus constituting a background for the understanding of the subsequent recommendations regarding pending lawsuits in the strict sense.

2. The rules should apply only to actions amenable to out-of-court settlement and to arbitration.

### **The effects of a judgment or arbitration award made prior to the liquidation**

3. A judgment or arbitration award that has gained legal force prior to the liquidation proceedings should be binding also in the proceedings, but only if it relates to a matter which the debtor, by means of contract, had been able to regulate with legal effect against the liquidation estate.

What is said in the first paragraph should not prevent recovery to the estate, in accordance with the provisions of Chapter VI, of the effects if a judgment or arbitration award is a result of collusion, procedural concessions, admissions or other procedural acts or omissions.

4. A judgement or award referred to in the previous section should not create any right to enforcement in the liquidation proceedings other than provided for in section III:5.

### **Pending lawsuits regarding assets**

*The insolvent side's right to continue or not to continue a lawsuit.*

5. The liquidation estate should have the right to choose between continuing a pending lawsuit in relation to an asset that may be subject to the liquidation seizure under section III:4, or not to continue with such lawsuit.

If the estate chooses to continue the lawsuit, the debtor should no longer be considered as a party to it.

6. The liquidation estate should, by way of exercising its right under the previous section, be represented by the trustee.

7. If the trustee chooses not to continue a lawsuit, a creditor should be entitled to do so as a party to the lawsuit but for the benefit of the estate.

The same should apply if the trustee is prepared to accept a settlement with a third party concerning the object of an out-of-court dispute and a creditor provides an adequate security for the total value of the settlement for the estate.

8. The right of a creditor to continue a lawsuit should not in any way limit the right of the trustee, in accordance with general rules, to sell or to abandon assets to the debtor in the liquidation.

9. If a creditor is successful in a lawsuit he has chosen to continue, he should be entitled to compensation for reasonable costs for the proceedings, however, only to such an extent that the estate will receive at least a net sum. If the creditor has provided security as outlined in section V:7 above, the net sum should at least amount to the value of the security provided.

10. If neither the trustee nor any creditor is willing to continue a lawsuit, it should continue with the debtor as party to the lawsuit, albeit for the benefit of the estate. The rules stated in sections V:7 paragraph 1, V:8 and V:9 above in respect of a creditor should then apply to the debtor.

11. A judgment or arbitration award, passed after the commencement of liquidation proceedings, should have the effect of *res judicata* in respect of the estate and the debtor irrespective of whether the trustee, a creditor or the debtor is continuing a lawsuit for the benefit of the estate as set forth in sections V:5-10.

#### *Information, stay of proceedings and notification*

12. The debtor should be obligated to provide notice of the liquidation to all relevant courts or arbitration tribunals dealing with lawsuits to which the debtor was a party at the time of the commencement of liquidation proceedings.

13. The court of law or the arbitration tribunal should be obligated to inform the trustee of any pending lawsuits concerning the debtor or the estate.

14. If the court of law or the arbitration tribunal fails to inform the trustee about pending lawsuits, the estate should not be bound by any decision or judgment or arbitration award in such a lawsuit.

15. The court of law or the arbitration tribunal should also be obligated to postpone any proceedings in order to give the estate adequate time to decide if the estate is to continue with the proceedings.

If the trustee considers not to continue a lawsuit, he or she should promptly notify the creditors accordingly along with the right of individual creditors to represent the interests of the estate in the lawsuit, and the time limits that must be observed in order to exercise that right.

16. If neither the trustee nor any creditor will, within a reasonable time specified in a court order, notify the court of law or the arbitration tribunal whether they intend to con

tinue the lawsuit, they should be considered to have refrained from exercising the right to continuation.

#### *Liability for costs*

17. If a trustee decides to continue a lawsuit on behalf of the estate, the estate should bear the risk for the costs of the proceedings accrued after the commencement of the liquidation proceedings. These costs should be considered as post-commencement claims. Costs accrued before the commencement of the liquidation proceedings should be considered as insolvency claims.

18. If the liquidation estate exercises its right not to continue a lawsuit, the estate should be able to do so without incurring liability for the costs of the proceedings.

19. A creditor or debtor who is continuing a lawsuit for the benefit of the estate as outlined above, should be liable for the costs of the proceedings. The estate should not be held responsible for such costs.

20. If the debtor continues a lawsuit as a party, after the commencement of liquidation proceedings,

- (a) the formal or *de facto* directors of the debtor, or
- (b) any other person who (i) supported the decision for the continuation of the lawsuit, or (ii) otherwise effectively contributed to the passing of the decision or execution thereof,

shall together with the debtor become jointly and severally liable for any cost of proceedings which have accrued after the date of commencement of liquidation proceedings. These costs will be imposed on the debtor.

If adequate security for the costs of the proceedings will be provided during the proceedings, the liability should be discharged. Should the security provided be insufficient, the liability should be limited to the insufficiency.

#### *Exceptions for certain legal systems*

21. In legal systems that do not allow the debtor to be represented by any other legal representative than the liquidator, the rules above should be modified as follows:

- (a) The debtor should not be a party to any lawsuit after the commencement of liquidation proceedings.
- (b) Lawsuits in which neither the liquidation estate nor any creditor participates should be dismissed.

### **Pending lawsuits regarding insolvency claims**

#### *Basic rules*

22. Pending lawsuits regarding insolvency claims should not automatically be dismissed but continue despite the commencement of liquidation proceedings.

The proof of debt procedure set out in Chapter VIII should not have the effect of *litis pendens* in respect of such lawsuits, and vice versa.



23. A judgment or arbitration award, that has gained legal force after the commencement of liquidation proceedings, should not create a right to a dividend in the liquidation.

However, a claim rejected in such a judgment or arbitration award should not entitle the creditor to a dividend in the liquidation.

Decisions and judgments in the proof of debt procedure should have no effect on pending lawsuits.

#### *Parties and interveners*

24. The debtor should always be considered as a party to a lawsuit which, in accordance with section V:22, continues in the liquidation proceedings, and the debtor should also have a right to continue them.

25. The estate represented by the trustee should have the right, in accordance with the rules set forth in sections V:26 and 27, to intervene in the debtor's lawsuit.

If the trustee chooses not to intervene, a creditor should be entitled to do so.

#### *Rights and obligations of the estate, individual creditors and the debtor*

26. If the estate or individual creditors choose to exercise the right to intervene, they should respectively have a right to *inter alia* bring forth new evidence, facts of legal grounds, and to continue the lawsuit, and to appeal without the consent of the debtor, to the same extent as a party to the proceedings.

27. A concession, a withdrawal of action or admittance of a fact in a lawsuit, by the debtor, the estate or a creditor, should not be binding on the debtor if the debtor, the estate or a creditor opposes such a concession or admittance of fact.

28. The rules stated in sections V:26 and 27 should not limit the rights to intervention under general procedural rules applicable to it.

#### *Rules on lawsuits regarding assets that should apply mutatis mutandis*

29. The rules on lawsuits regarding assets in sections V:12-21 should apply mutatis mutandis to lawsuits concerning insolvency claims, with the following modifications:

(a) As regards the application of sections V:17-19, if the estate or an individual creditor exercises the right to intervene in a lawsuit, the debtor alone should be liable for the costs accrued before the intervention and the intervener together with the debtor should be jointly liable for the costs accrued after the request to intervene.

(b) As regards the application of section V:20, the liability should be excluded *ex nunc* if the debtor motions the court for a withdrawal of the action and the lawsuit continues due to the intervention of the estate or a creditor.

## VI. Recovery to the estate

### General description of the rules

1. Insolvency law should include rules that make it possible for the estate to recover legal transactions undertaken within certain time limits before the insolvency proceedings were commenced.

2. General conditions for recovery should be that the transaction in question has caused a disadvantage for one or more of the creditors and could not have been undertaken in a legally binding way, if the debtor at the time of the transaction already had been put into insolvency proceedings.

3. The recommended rules are based on both a general rule applicable to all types of legal transactions and containing subjective elements, and a set of rules for certain types of transactions with purely objective elements. The general rule is meant to be used independently of the specific rules, and vice versa.

### Calculation of the time limits for recovery

4. In the recommended rules the time limits for recovery are formulated in terms of the transaction in question, must have taken place “*later than*” a certain period of time before the critical date. The quoted expression covers both transactions carried out within a certain period of time before and after this date.

“*Critical date*” refers to the date an application for liquidation was submitted to the court. According to section I:7, if a preceding reorganisation has been converted to the current liquidation, or if the application for liquidation has been made within two months from the time a previous reorganisation had been completed, then “*critical date*” should refer to the date of application for reorganisation.

### Related persons

5. The recommended rules provide extended opportunities to recover transactions in cases where the debtor’s counterparty is related to the debtor.

With regard to individuals, the term “*related person*” should mean a person who is married to the debtor or is a sibling or is a direct ancestor or descendent of the debtor or is related through marriage to him by a direct descendent or ancestor or where one is married to the other’s sibling as well as a person who in another way is particularly close to the debtor.

Furthermore, where the debtor is a corporation or other legal entity the term “*related person*” should mean:

(a) a person who has a substantial joint interest with the debtor based on entitlement to a share or a comparable financial interest,

(b) a person who not alone but together with a related person has such a joint interest with the debtor as mentioned in (a),

(c) a person who, by a formal or informal management position, has a decisive influence over the activities conducted by the debtor, or

(d) a person who in turn is related to someone who is related within (a) - (c).

### **The effects of recovery**

6. The network does not address the detailed legal effects of a successful action for recovery. However, the basic principle should be that the recovery, at least in financial terms, recreates the situation that would have existed if the recovered transaction had never taken place.

7. If property that may be recovered has been transferred to a third party, an action for recovery should be possible against the third party, if he knew or should have known of the facts forming the basis for the right to recovery against the transferor.

### **Preconditions for recovery**

#### *General rule*

8. A legal transaction, carried out later than five years before the critical date, whereby

- (a) a particular creditor has been improperly favoured in preference of others,
- (b) an asset of the debtor has been improperly concealed from the creditors, or
- (c) the debtor's debts have been improperly increased,

is to be recovered if the debtor was or by way of the transaction, solely or in combination with other circumstances, became insolvent and the counterparty knew or ought to have known (was in "bad faith") of the insolvency of the debtor and the circumstances making the transaction improper.

A related person should, for the purposes of the first paragraph, be deemed to be in bad faith unless it is shown that he probably neither knew or ought to have had such knowledge.

#### *Undervalued transactions*

9. A gift is to be recovered, if it has been completed later than one year before the critical date.

A gift to a related person is to be recoverable even if it has been completed earlier but no later than three years before the critical date, unless the recipient can prove that the debtor after the gift obviously remained solvent or retained assets to a value that clearly could meet his debts.

The preceding paragraphs should also apply to sales, exchange or other contracts if, having regard to the disproportion between the consideration of the respective parties, it is obvious that the contract was in part in the nature of a gift.

Support and customary gifts that were not disproportionate to the financial situation of the debtor should be excluded from recovery under this section.

### *Payments and corresponding transactions*

10. A payment of a debt that occurred later than three months before the critical date is to be recoverable, if it was made

- (a) with something other than customary means of payment,
- (b) prematurely, or
- (c) in an amount that resulted in a significant deterioration in the debtor's financial position or liquidity,

unless it can nevertheless, having regard to the circumstances, be considered ordinary.

A payment to a related person is to be recoverable even if it was made earlier but later than two years before the critical date, unless the recipient can prove that the debtor neither was, nor by the payment became, insolvent.

The previous paragraphs should also be applied when a set-off has taken place, and when a non-monetary obligation has been performed.

### *Securities*

11. A security that the debtor has transferred later than three months before the critical date is to be recoverable, if

- (a) the security was not agreed when the debt was created, or
- (b) the security was transferred with delay after the debt was created,

unless the transfer can nevertheless, having regard to the circumstances, be considered ordinary.

A security transfer to a related person is to be recoverable even if it was made earlier but no later than two years before the critical date, unless the recipient can prove the debtor neither was, nor by the transfer became, insolvent.

Other measures undertaken in order to protect the security right against third parties, is to be treated as the equivalent to a transfer of security.

### *Attachments*

12. A priority right or payment, which a creditor has gained by attachment later than three months before the critical date, is automatically to be recovered.

If an attachment was made for the benefit of a related person, the priority right or payment is to be recovered even if the priority right arose earlier but no later than two years before the critical date, unless the creditor can prove that the debtor neither was, nor became insolvent as a result of this measure.

### **Actions for recovery**

13. The trustee is to have the primary right to initiate a recovery action for the benefit of the estate. This right he or she may exercise by:

- (a) instituting proceedings in a general court,
- (b) making an objection to a submitted claim or in connection with distribution proceedings, contest the claim in other procedures concerning payment or priority rights in the liquidation, or

(c) making an objection against another application presented in a lawsuit against the estate.

14. If the trustee chooses not to demand recovery and a settlement in the matter is not made, a creditor should be entitled to require recovery by initiating a lawsuit in a general court.

In such a lawsuit, the creditor should act as a party albeit for the benefit of the estate. The creditor should then be responsible for the costs for the proceedings but should be entitled to obtain compensation from the estate for the costs incurred, to the extent that the expense covers the benefit accruing to the estate as a result of the lawsuit.

15. A recovery action in a general court may be initiated within one year from the commencement of the liquidation proceedings. An action may also be initiated within six months when the material grounds for a claim become known to the liquidation estate.

### **Recovery in reorganisation proceedings**

16. The recommended rules above should also be applicable in reorganisation proceedings.

17. The primary right to initiate a recovery action should be exercised primarily by the administrator or otherwise by a creditor, whose rights could be affected by the reorganisation plan.

In such lawsuits the administrator and the creditor, respectively, should act as a party albeit for the benefit of the affected parties in the reorganisation.

## **VII. Insolvency claims**

### **Basic rules**

1. An insolvency claim is a claim that should be recognised and form part of the insolvency proceedings and

(a) in liquidation, be paid only in accordance with the priority order,

(b) in reorganisation, if not fully secured could be affected by the debt settlement in the reorganisation plan.

2. A claim should be an insolvency claim if it had arisen, in liquidation, prior to the proceedings being commenced and, in reorganisation, prior to the application to commence the proceedings. This should apply even if the claim is dependent upon conditions or is not yet due for payment.

### **Additional rules regarding insolvency claims which are dependent on conditions**

3. If an insolvency claim is dependent on a condition whereby the creditor is not entitled to receive the amount of the claim unless a certain event occurs, distribution for the claim should not be computed in a distribution proposal if there is no reason to assume that the condition will be satisfied.

Distribution for a claim referred to in the first paragraph may not be paid out before the condition has been satisfied. However, funds for future payment should not be kept in reserve for a period longer than ten years.

### **Interest on insolvency claims**

4. For unsecured insolvency claims, interest between the creditors should be calculated after the commencement of the insolvency proceedings only if the estate is sufficient to pay more than the amount of all insolvency claims that are not secured.

### **Claims for specific performance**

5. A claim for specific performance should, irrespective of whether it concerns a monetary or non-monetary obligation, be able to participate in the insolvency proceeding, but it is only with the monetary claim that the creditor would have had if the contract or other legal relationship on which the claim is based had been cancelled by the creditor at the commencement of the proceedings. However, this should not apply to a claim under a contract that the insolvent side has chosen to continue in accordance with the rules set forth in Chapter IV above.

## **Set-off with insolvency claims**

### *Basic rule*

6. An insolvency claim may be used by the creditor to set-off a claim that the debtor had against him when the insolvency proceedings commenced. However, this should not apply if a set-off was excluded outside the proceedings by reason of the nature of the claim.

### *Specific restrictions on the right to set off*

7. An insolvency claim acquired by a transfer from a third party up to three months before the critical date stated in section VI:4, may not be used as a set-off against a claim which the debtor had when the creditor acquired his claim. This should also apply if the insolvency claim had been previously transferred from a third party and the creditor was in bad faith with regard to the debtor being insolvent.

A creditor who has been indebted to the debtor in circumstances equivalent to payment by means other than the customary means of payment, should not be entitled to set-off to the extent that such payment could have been subject to recovery.

## **VIII. The order of priority regarding insolvency claims**

### **Basic rules**

#### *Liquidation*

1. Insolvency law should establish an order of priority, stating how the proceeds of the debtor's assets shall be distributed between different classes of creditors holding insolvency claims.

#### *Reorganisation*

2. Regarding reorganisation, the issue of satisfaction of creditors holding insolvency claims should be regulated under the rules relating to the reorganisation plan's content, approval and confirmation. In this set of recommendations, these issues are addressed in sections XII:4-10.

### **Secured claims**

3. A secured claim should be satisfied from the proceeds of the security. The secured value should be protected as provided for in sections III:9-10.

To the extent that the proceeds of the security are insufficient to satisfy the secured creditor's claim, the creditor may participate in the proceedings as an unsecured creditor unless he has agreed to adhere only to the security.

### **Unsecured claims**

4. A basic principle should be that all unsecured creditors are equally entitled to payment in relation to the size of their claims (*pari passu*). Very strong reasons must exist for legislative deviations to be considered acceptable.

5. If there are different classes of unsecured claims, all creditors in a class with a higher priority should be fully paid before creditors in the next class are paid.

6. It should, by virtue of law or contract, be possible to rank certain claims below ordinary unsecured claims (*subordinated claims*). In the insolvency proceedings, such a subordination should be recognised regardless of whether it has been made in relation to all or certain other creditors.



## **IX. Proof of debt procedure**

### **Basic rule regarding liquidation**

1. If unsecured creditors are expected to receive a dividend in the liquidation, the trustee should be obligated to request that a procedure for submission of claims and presenting objections to claims ("*proof of debt procedure*") is to be held by the court.

### **Submission of unsecured insolvency claims**

#### *Liquidation*

2. The time period for submission of claims should extend between four and ten weeks from the day of the court's decision to initiate a proof of debt procedure.

A creditor should be able to participate in the proceedings even if he submits his claim after the expiry of the period specified in the first paragraph. The creditor should in such cases be charged a reasonable fee by the court.

3. If a creditor fails to submit his claim before the trustee's distribution proposal has been subject to public notice by the court, the creditor should lose his right to participate in the liquidation.

#### *Reorganisation*

4. If a claim is not already known, the creditor should be able to notify his claim to the administrator two weeks at the latest prior to the creditor's meeting in which the plan will be voted.

5. If a creditor fails to submit his claim within the time specified in the preceding section, the creditor should not be entitled to vote on the reorganisation plan and be considered as an unknown creditor. Like other unknown creditors, the creditor in such cases should lose his right to payment by the debtor, unless his claim would not have been affected by the plan or otherwise provided for in the plan.

### **Objections to insolvency claims**

#### *Scope*

6. The contents of the following sections regarding objections to claims is also intended to cover objections to claimed priority rights and rights to set off.

#### *Liquidation*

7. The trustee, a creditor and the debtor should be able to present objections to a submitted claim. If the trustee finds cause to object to a claim, he or she should be obligated to do so.

An objection should be addressed to the trustee during a time period set by the court which should extend between two to four weeks after the end of the proof of debt procedure.

8. If one or several claims have been the subject of objections, the court should hold a meeting in order to settle the dispute. If the parties are not able to reach a settlement, the question in dispute should be determined by the court in a simplified procedure with legal effect only as to the matters affected by the liquidation.

### *Reorganisation*

9. The administrator, the debtor and a party whose rights are proposed to be altered by the reorganisation plan should be able to present objections to a claim. If the administrator finds cause to object to a claim he or she should be obligated to do so.

An objection presented by the debtor or an affected party should be addressed to the administrator at the latest one week before the creditors' meeting on voting on the plan. The administrator should, if it is deemed reasonable and feasible, try to achieve that all disputes have been resolved prior to this meeting taking place.

10. If one or several claims have been subject to objections, and the dispute has not been settled, the court should endeavour to settle the dispute at the creditors' meeting on voting on the plan. If the parties are not able to reach a settlement, the question in dispute should be determined by the court in a simplified procedure with legal effect only as to the matters affected by the plan.

## **X. Treatment of post-commencement claims**

### **Basic rules**

1. A post-commencement claim should be met in full in the insolvency proceedings, either according to the cash principle or as it becomes due.

2. In the event of liquidation, post-commencement claims are against the estate as a special legal entity or should have a priority that corresponds to this ("*mass claims*").

The mass claims should provide the right to attachment and other enforcement against the estate. They could also be used to put the estate into liquidation or initiate an equivalent settlement.

3. In reorganisation, post-commencement claims should not be covered by the payment suspension, the stay of enforcement proceedings and should not be subject to the debt settlement in the reorganisation plan.

If the reorganisation is immediately or after a specified period of time followed by liquidation, the post-commencement claims from the reorganisation should be protected as a top priority unsecured insolvency claim.

### **Grounds for post-commencement claims**

4. The assessment as to whether a claim is a post-commencement claim should be made according to the same principles for liquidations and reorganisations.

A claim should be a post-commencement claim if it is based on

(a) a commitment that the liquidation estate or the debtor in reorganisation duly made after the commencement of the proceedings,

(b) a liability which the liquidation estate or the debtor in reorganisation has otherwise incurred after the commencement of the proceedings, or

(c) the liquidation estate's or the debtor's in reorganisation consumption or use of a performance which a creditor or party at the commencement of the proceedings had a protected right to withhold or withdraw.

## **XI. Administration of insolvency proceedings**

### **Basic rules**

#### *Liquidation*

1. The trustee's primary duty is to address the joint interests of the creditors. To accomplish this task, the trustee should have the exclusive authority to perform legal acts and bring actions on behalf of the estate. The debtor must be required to assist the administrator in various ways during the proceedings.

The administration of the estate should be subject to public supervision. The supervision should be carried out by a competent unit at, or by a judge, of the court in which the proceedings are pending, or by another authority.

#### *Reorganisation*

2. For a reorganisation the principle according to section III:2 should be that the debtor himself would manage the administration. However, an administrator should be appointed whose principal tasks would be to review the debtor's financial situation and business, assist the debtor with his reorganisation work, supervise the debtor in the interest of the creditors, provide or withhold consent to transactions such as those the debtor is not permitted to conduct, provide the creditors and the court with information, determine the prospects for a successful reorganisation and to initiate that the reorganisation proceedings will be set aside when reasons for so-doing exist. The debtor should be obligated to give information to the administrator, on request.

3. In a reorganisation where the right of disposition has been taken away from the debtor according to section III:3, it should either be taken over by an administrator or by a trustee after the reorganisation, according to section I:7, has been converted to liquidation.

The administration of a reorganisation where the administrator has assumed the right of disposition should be subject to the same public supervision as with liquidations.

### **Qualification requirements for liquidation trustees and reorganisation administrators**

#### *General requirements*

4. The same requirement for insight, experience and suitability for handling the proceedings in question should apply to a liquidation trustee as to a reorganisation administrator. In most jurisdictions this would normally be a lawyer. The network does not consider whether requirements for certain formal qualifications, a specific title, certification or license should be made in addition to the general suitability requirement.

5. The same requirement for independence and impartiality in relation to both the debtor and the creditors should apply for both categories. The trustee or administrator

should be obligated to declare if there exists any threats to independence or any conflict of interest.

*Could the administrator be appointed liquidation trustee regarding the same debtor in a subsequent reorganisation?*

6. The question of whether the administrator could be appointed trustee in a subsequent liquidation is to a certain degree dependent on the administrator's role in the reorganisation and whether measures and legal transactions taken during the reorganisation following a decision by, or with the consent of, the administrator may be challenged in the liquidation. A key task of the administrator should be to initiate that the reorganisation proceedings will be set aside when grounds for this exist, and negligent omission in this regard should form the basis for liability. Therefore, the clear main rule should be that a person other than the former administrator is to be appointed. Exceptions should only be made in special circumstances when, for example, the reorganisation has been underway for just a few days and nothing of significance has occurred.

### **Appointment and dismissal of the trustee and the administrator**

7. Both the trustee or the administrator should be appointed by the court.

8. There should not be a requirement, but an option, in the application to put forward a proposal for a specific person to be appointed liquidations trustee. The trustee should in principle always be appointed irrespective of any proposals. If it is evident from the application that a person who has been proposed fulfils the suitability requirement, and there is no noteworthy objection to this, the court should be able to approve the proposal without further consideration.

An administrator in reorganisation should be appointed after a proposal by the applicant. However, as in liquidations, the court should not be bound by the proposal, but should be able to approve it under the same guidelines as for liquidations.

9. The trustee and the administrator could be dismissed by the court at the request of a creditor, a creditors' meeting, a creditors' committee, the debtor, the trustee or administrator him or herself or ex officio. In cases where the proceedings are subject to public supervision; such a request could also be made by the supervisory authority. The reason for the dismissal should be that the requirements under sections XI:4 and 5 are not met or that the trustee or administrator for some other reason should be dismissed from the assignment.

### **The decision-making power of the trustee and the administrator contra the creditors in management issues**

#### *Liquidation*

10. The trustee should have the right to independently make decisions and take action on management issues. For important matters, however, the administrator should have a duty to consult with those creditors who would be particularly affected.

Creditors' meetings and creditors' committees can exist, but should not have the right to make binding decisions on management issues, unless otherwise expressly stipulated.

### *Reorganisation*

11. For reorganisations the starting point according to sections III:2 and XI:2 should be that the debtor has the right to make decisions and take action with regard to the management, and the administrator's right to make decisions is essentially limited to either providing or withholding consent to transactions that the debtor, by way of exception, is not permitted to conduct and to initiate the termination of the proceedings. As with liquidations, the administrator should have a duty to consult ahead of important decisions with those creditors who are particularly affected and, in addition, consult with the creditors' committee if one has been appointed.

For reorganisations where the administrator has taken over the right of disposition pursuant to section III:3, the right to make decisions should be equal to what is pursuant to section XI:10 with regard to liquidations.

### **The trustee and administrator's liability for damages**

12. A trustee and an administrator should have a duty to compensate for damage that he or she intentionally or negligently caused with regard to either the estate, a creditor or the debtor whilst performing his or her duties.

According to the first paragraph there should also be liability against third parties provided the trustee or the administrator has disregarded a written or unwritten insolvency law rule laid down for the protection of third parties.

### **The court's qualifications and role in the management**

13. Insolvency proceedings, as well as other cases and matters with strong insolvency law implications, should be handled by insolvency courts, commercial courts with special qualifications in the area of insolvency law, or by a division of a court or certain judges who are specialised in or equipped with special qualifications in insolvency law.

14. If the qualification requirements in the previous section's conditions cannot be met, the insolvency law should not give the court a central or an active role in the management of liquidation or reorganisation proceedings.

## **XII. The reorganisation plan**

### **General description**

1. During reorganisation proceedings a reorganisation plan should be drawn up to be presented to the creditors for approval and confirmation by the court. The plan should include the legal and actual measures considered necessary and possible to carry out in order to continue the debtor's business or parts thereof in a profitable and sustainable way.

### **Who should present the plan?**

2. The plan should be drawn up and presented by either the debtor or the administrator. The administrator shall, in the former case, assist the debtor in the process of drafting the plan.

If the proceedings are commenced without the debtor's consent, as referred to in section I:4, the administrator shall present the plan.

### **When should the plan be presented?**

3. As stated in section I:16, a preliminary reorganisation plan should be included in the application for reorganisation.

A final reorganisation plan should be presented to the creditors within a specified time from the commencement of the proceedings. This period should not be less than two months and no longer than six months. However, the court should, at the request of the debtor or the administrator, be able to extend this period by two or three months at a time up to a maximum of twelve months, taking into account the size or complexity of the debtor's business, or if there are other special reasons to prolong the proceedings.

Irrespective of the time periods specified in the second paragraph, the reorganisation could be set aside, and the proceedings converted into liquidation under those conditions set out in section I:7.

### **Content of the plan**

4. The content of the reorganisation plan should not be heavily regulated and thus the plan could contain optional features. However, the reorganisation plan should contain information about

(a) the debtor's business and an analysis of the reasons behind the debtor's financial difficulties,

(b) the legal and actual measures which have been carried out during, and will be necessary to carry out after the proceedings in order to address the difficulties of the debtor or the business, and which are required in order for the business or parts thereof to be continued with sustainable profitability by the debtor or someone else. This may include a composition proposal, changes in personnel, changes in contracts, changes in structure of ownership, etc.

- (c) the financing of the plan and the continued operation of the business,
- (d) a timetable for implementation of the measures set out in the plan, and
- (e) a classification of the creditors and equity holders, whose rights are altered by the plan (“*the affected parties*”), in voting groups on the plan.

5. The voting groups mentioned in the previous section should consist of affected parties with similar interests. These groups should, in turn, be possible to divide into separate groups of affected parties whose claims have substantially the same basis.

The purpose of using this kind of group system is to achieve maximum flexibility and enable creative, but also legally binding arrangements with and within different classes of creditors and equity holders in a more differentiated way than can be achieved through the mere application of the order of priority in liquidation. This system should provide the possibility, for example, to convert debts to equity or allowing a group of creditors to receive other non-monetary assets to a value equal to what another group with the same priority will receive in cash.

6. The reorganisation plan should be accompanied by various documents regarding the debtor and the business, a list of liabilities and assets and the value of these, a statement made by the administrator regarding the prospects of a successful implementation of the measures specified in the plan and an assessment of the expected dividend in the event of liquidation.

### **Approval of the plan**

7. The plan should be approved by the affected parties by way of a vote. The voting should take place in the groups mentioned in section XII:4 (e) and 5 above. Within these groups, voting should be based on the principle of simple majority with respect to both the number of the voting parties and the amount of their claims.

8. If a creditor is partially unsecured, he should be able to vote in relation to the unsecured claim. The valuation of the security should, as the valuation of other assets, be carried out by the administrator but should be possible to challenge in court by the partially secured creditor, other affected parties and the debtor in connection with an appeal of the confirmation of the plan as a whole. The objective of the valuation should be to determine a realistic market value of the security and should refer to the security as it existed at the commencement of the proceedings. This value should correspond to the price for which the security could have been sold in a liquidation, either as part of an ongoing business or separately, depending on which option seems the most likely in the particular case.

### **Confirmation of the plan**

9. If the required majority of each voting group has approved the plan, it should be subject to confirmation by the court to gain legal effect. This means that the affected parties’ rights are altered to the extent and in the manner specified in the plan.

Even if the required majority has not been met in any of the voting groups, the court should be able to confirm the plan if the affected parties of the group in question are



treated in a way that can be considered fair and equitable. This requirement should be regarded as fulfilled, if

(a) no creditor or equity holder receives an economic value from the plan that exceeds the full amount of his claim,

(b) no creditor or equity holder with lower priority than the group that voted against receive an economic value from the plan,

(c) no creditor or equity holder with the same priority that the group that voted against receives a higher economic value from the plan than this group, and

(d) the plan has received support in a majority of the voting groups.

10. Regardless of whether the plan has received support of a majority of each voting group or not, it should not be confirmed if an affected party who has voted against the plan makes it likely that the economic value he receives from the plan is less than the dividend he would have received in the event of liquidation.

### **Supervision**

11. There should be rules regarding supervision of the plan during the period of its implementation. The supervision should be exercised by the administrator or another appropriate person.

The tasks of the supervisor should be to ensure that the measures set out in the plan are implemented on schedule, assist the debtor in his implementing work, provide the affected parties with information relevant to the implementation and request that the plan is terminated in accordance with section XII:13 below.

As regards rights to information, qualification requirements, appointment, dismissal and liability for damages, the same rules should apply for the supervisor as for the administrator.

### **Amendment of the plan**

12. A confirmed reorganisation plan should be altered only with the consent of the party or parties whose rights under the plan would be affected in a negative way by the amendment.

Notwithstanding the first paragraph, a confirmed reorganisation plan may be altered due to changes in the circumstances upon which the plan was drafted according to general principles of contract law.

### **Termination of the plan**

13. At the request of the supervisor or any affected party, the court should be able to decide on the termination of a confirmed reorganisation plan, if the debtor grossly breaches his obligations under the plan.

The effect of a termination should be that the affected parties have the same rights against the debtor and other parties as if the plan had never been confirmed. However, the termination does not affect legal acts that have already been made.

What is stated in the preceding paragraphs should also apply in the event the debtor is put into liquidation before the measures set out in the reorganisation plan have been implemented, provided that what remains to be carried out is not of minor importance.

### **XIII. Treatment of environmental claims in insolvency proceedings**

#### **Basic rules**

1. Insolvency law should provide rules which clarify how claims raised by environmental authorities on the prevention or remedying of environmental damage caused by the debtor's business ("*environmental claims*") should be treated in insolvency proceedings.

2. The rules regarding environmental claims should be based on the general applicable rules regarding insolvency claims and post-commencement claims, unless otherwise specified.

#### **Environmental claims that constitute insolvency claims**

3. Environmental claims based exclusively on the debtor's acts or omissions prior to the commencement of insolvency proceedings should constitute insolvency claims.

4. Environmental claims which have arisen in connection with preventive or remedial measures taken to real property or other affected assets, should have the best right to payment from the proceeds of these assets. This should apply regardless of whether the measures have been taken before or after the commencement of the insolvency proceedings.

5. To the extent the proceeds from the assets referred to in the previous section are insufficient to satisfy the environmental claims, the environmental authority may participate in the proceedings with an unsecured insolvency claim.

The network chooses not to address the purely political question, whether there may be reasons strong enough to grant such an unsecured claim priority over other unsecured claims in the insolvency proceedings.

#### **Environmental claims that constitute post-commencement claims**

6. If the debtor's business is continued by the liquidation estate or the debtor in reorganisation, the new or additional environmental claims, which arise as a result of the continuing operations, should constitute post-commencement claims.

#### **Notification to the environmental authority**

7. The liquidation trustee and the reorganisation administrator should have a duty to notify the environment authority if it is discovered or there is reason to believe that the debtor has produced chemical products, biotechnological organisms or hazardous waste that need to be disposed of. The same should apply in cases of suspected contamination of land or water pollution.

## **XIV. Treatment of groups of companies in insolvency proceedings**

### **General scope of the rules**

1. Insolvency law should provide rules that enable efficient and effective management of insolvency proceedings regarding groups of companies.

These rules should be based on the general applicable rules regarding insolvency proceedings, unless otherwise specified.

2. The term “*group*” should in this context mean the same as set out in Directive 2013/34/ EU of the European Parliament and of the Council of 26 June 2013 on the annual financial statements, consolidated financial statements and related reports of certain types of undertakings, amending Directive 2006/43/EC of the European Parliament and of the Council and repealing Council Directives 78/660/EEG and 83/349/EEC.

The term “*group member*” refers generally to both the parent company and the subsidiaries, in accordance with the directive mentioned above.

3. The vast majority of the rules recommended below are based on each group member retaining its legal identity in the insolvency proceedings, as well as its own assets and liabilities.

In certain exceptional cases, however, it is recommended below that this basic position is waived and that two or more group members’ assets and liabilities could be treated as if they were part of the same estate (“*substantive consolidation*”).

### **Joint application**

4. A joint application to commence insolvency proceedings may be made with respect to two or more group members, provided that the requirements for commencement are met for each member. When the application is made by a creditor, he should have claims against all members concerned.

### **Joint insolvency court**

5. At the request of one or more group members, or by a creditor, separate insolvency proceedings regarding two or more group members should be dealt with in the same insolvency court, if it is appropriate to have a joint process and the joint court in question has jurisdiction for at least one of the interested group members.

If a request for a joint court is made after one or more insolvency proceedings have been commenced, the transfer of the proceedings should require the consent of the liquidation trustee or reorganisation administrator. In such cases, the trustee or administrator should also be able to initiate a transfer of the proceedings.

### **Joint trustee and administrator**

6. A person who shall be or already has been appointed liquidation trustee for a group member should be appointed as trustee also for one or more additional members of the same group, where this is appropriate with regard to the management of the affected estates.

However, a joint trustee should not be appointed under the first paragraph, if there are reasons to believe there will be conflicts of interest that would significantly complicate the performance of the assignment and whereby the conflict of interest cannot be resolved by one or more co-trustees being appointed within defined themes.

7. The recommended rules on joint liquidation trustees should also be applicable to reorganisation administrators.

### **Cooperation and communication**

8. The Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on insolvency proceedings (recast) includes in Articles 56-59, as regards cross-border group insolvency cases, a set of rules on cooperation and communication between insolvency practitioners, between courts and between insolvency practitioners and courts, as well as treatment of the costs of such cooperation and communication. – Corresponding rules should apply to domestic group insolvency cases.

### **Intra-group financing in insolvency proceedings**

9. It should be permitted in the relationship between two or more group members, each of which is subject to insolvency proceedings, to provide and obtain new financing, securities for new financing and guarantees or other assurances for new financing. Pre-requisites for this should be that the measure in question, with regard to all involved group members, is necessary for the continued operation or survival of the business or for the preservation or enhancement of the value of the estate.

If a measure in accordance with the first paragraph is detrimental for an individual creditor or group of creditors, it should still be permitted if the measure in question has obvious benefits for the general body of creditors of the same estate, and these benefits have a substantially higher value than the disadvantage for the affected individual creditor or group of creditors.

10. As regards the priority and other treatment of intra-group financing, the general rules on post-commencement claims should be applied, see Chapter X above.

### **Group perspective on recovery of internal transactions**

11. For the purposes of the recommended rules on recovery to the estate in Chapter VI, the group context should be taken into account when assessing whether a transaction should be considered improper (section VI:8) and ordinary (sections VI:10 and 11). Otherwise, the group context should not, as long as it has not been decided on substantive

consolidation, involve considerations other than those that generally should be made in connection with an action for recovery to the estate.

### **Joint or coordinated reorganisation plan**

12. A joint or coordinated reorganisation plan involving two or more group members should be possible to present for approval by the creditors and confirmation by the court.

A group member who is not the subject of a reorganisation that has been commenced in accordance with the rules in Chapter I above, should, however, not be able to participate in a joint or coordinated reorganisation plan to be approved by the creditors and confirmed by the court if this would lead to a deterioration of the rights of creditors or other affected parties who have not given their consent to such a plan.

### **Substantive consolidation**

#### *Application*

13. A person, who under the general rules of sections I:1-3 has the right to make an application for commencement of insolvency proceedings, should also be permitted to make an application to the court for substantive consolidation concerning two or more group members. After insolvency proceedings have commenced, the trustee in liquidation and the administrator in reorganisation should have the same right.

#### *Prerequisites*

14. The court should decide on substantive consolidation if either of the following two criteria are met:

(a) The assets or liabilities of the group members are intermingled to such an extent that it would entail disproportionate costs or unreasonable delay to identify who owns the assets or is responsible for the liabilities.

(b) Group members are used as tools for fraudulent transactions without legitimate business purpose, and substantive consolidation is essential to rectify these transactions and limit the damage they have caused the creditors or other affected parties in the insolvency proceedings.

#### *Scope of consolidation*

15. The scope of the substantive consolidation should correspond to the extent to which assets or liabilities have been intermingled, or fraudulent transactions have been carried out, in accordance with the criteria for consolidation under the previous section.

At the request of a person who is entitled to apply for substantive consolidation under section XIV:13, the court may also decide to exempt specified assets and claims from consolidation.

#### *General effect of consolidation*

16. The court's decision on substantive consolidation should have the effect that the assets and/or liabilities of the concerned group members are to be treated as if they were

part of the same estate. This effect entails, with regard to consolidation of debts, that claims and debts between the group members are extinguished in the proceedings and that all claims against group members are treated as if they were insolvency claims in a single insolvency proceeding.

#### *Effects on the order of priority*

17. The general rules regarding the order of priority should, in cases where the consolidation includes both assets and liabilities, be applied with regard to all assets and debts subject to consolidation. Security interests are to be respected and the priorities established in relation to an individual group member are to be recognised also in relation to competing priorities established in relation to other group members, as if all priorities had been established in relation to the same group member. However, a creditor who had lower priority than another creditor prior to the decision on substantive consolidation, should also be subordinated to the other creditor after the decision.

#### *Calculation of the time limits for recovery*

18. When substantive consolidation has been decided for two or more group members, and the rules on recovery to the estate shall be applied, the “*critical date*” in Chapter VI should refer to a common date for all group members. This date should be the date on which the first application for the commencement of insolvency proceedings was made.

## **XV. Short-term protection of voluntary restructuring negotiations**

### **General stay of enforcement proceedings**

1. As a protection of voluntary restructuring negotiations, a debtor should be entitled to request a court to grant a temporary stay of enforcement actions and insolvency proceedings with the effects equivalent to those provided for in sections III:7–9.

### **Selective stay of enforcement proceedings**

2. As an alternative to a general stay under the previous section, the debtor should be entitled to initiate a selective stay of enforcement proceedings by raising an objection against an individual enforcement action or insolvency proceedings that has already been initiated.

### **Prerequisites for the stay**

3. The stay referred to in the previous paragraphs should be granted only if the debtor makes it probable that

- (a) the negotiations have a reasonable prospect of leading to a sustainable settlement,
- (b) the debtor is able to pay all debts arising after the stay is granted, and
- (c) counterparties to the debtor's contracts, creditors holding security interests and other interested parties, which in a formal reorganisation would have been provided with adequate protection of their interests, cannot be expected to suffer any significant loss as a result of the stay.

### **Duration and lifting of the stay**

4. The stay should not be granted for a period longer than two months.

5. The court or the executive authority that has granted the stay should be required to fully or partially lift the stay at the request of the debtor or a creditor who is affected by it. In the latter case, the conditions for lifting the stay should correspond to the conditions for early termination of a formal reorganisation. In this set of recommendations, these issues are regulated in section I:7, first paragraph.

### **Prohibition of ipso facto clauses**

6. Counterparties to the debtor's contracts should not be entitled to withhold performance, terminate contracts or accelerate contracts with reference to the protected negotiations, the debtor's request for a stay, the decision to grant a stay as such or any similar event connected to the stay.



### **Priority for new financing**

7. New financing obtained during the stay should in a subsequent liquidation be afforded a priority that corresponds to what is recommended for post-commencement claims from a formal reorganisation under section X:3, second paragraph.

### **Calculation of the time limits for recovery in a subsequent liquidation**

8. If an application for liquidation is made within two months from the time a previous stay under this chapter was last completed, the critical date for recovery to the liquidation estate under Chapter VI should refer to the date the stay was initiated under section XV:1 or 2 above.

### **Application of the rules regarding the reorganisation plan**

9. The rules regarding the reorganisation plan in Chapter XII should be available also to debtors who are involved in voluntary restructuring negotiations. The following modifications from the generally recommended rules should then apply:

(a) The term “*reorganisation proceedings*” refers to the rules on the reorganisations plan’s presentation, content, approval and confirmation (“*the plan proceedings*”).

(b) The term “*commencement of the reorganisation proceedings*” refers to the date when a final reorganisation plan was presented (“*commencement of the plan proceedings*”).

(c) The term “*insolvency claim*” refers to a claim that has arisen before the commencement of the plan proceedings.

(d) The term “*post-commencement claim*” refers to a claim that has arisen after the commencement of the plan proceedings.

(e) The term “*administrator*” shall, for the purposes of Chapters IX and XI, refer to the court.

# Nordic-Baltic Insolvency Network

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