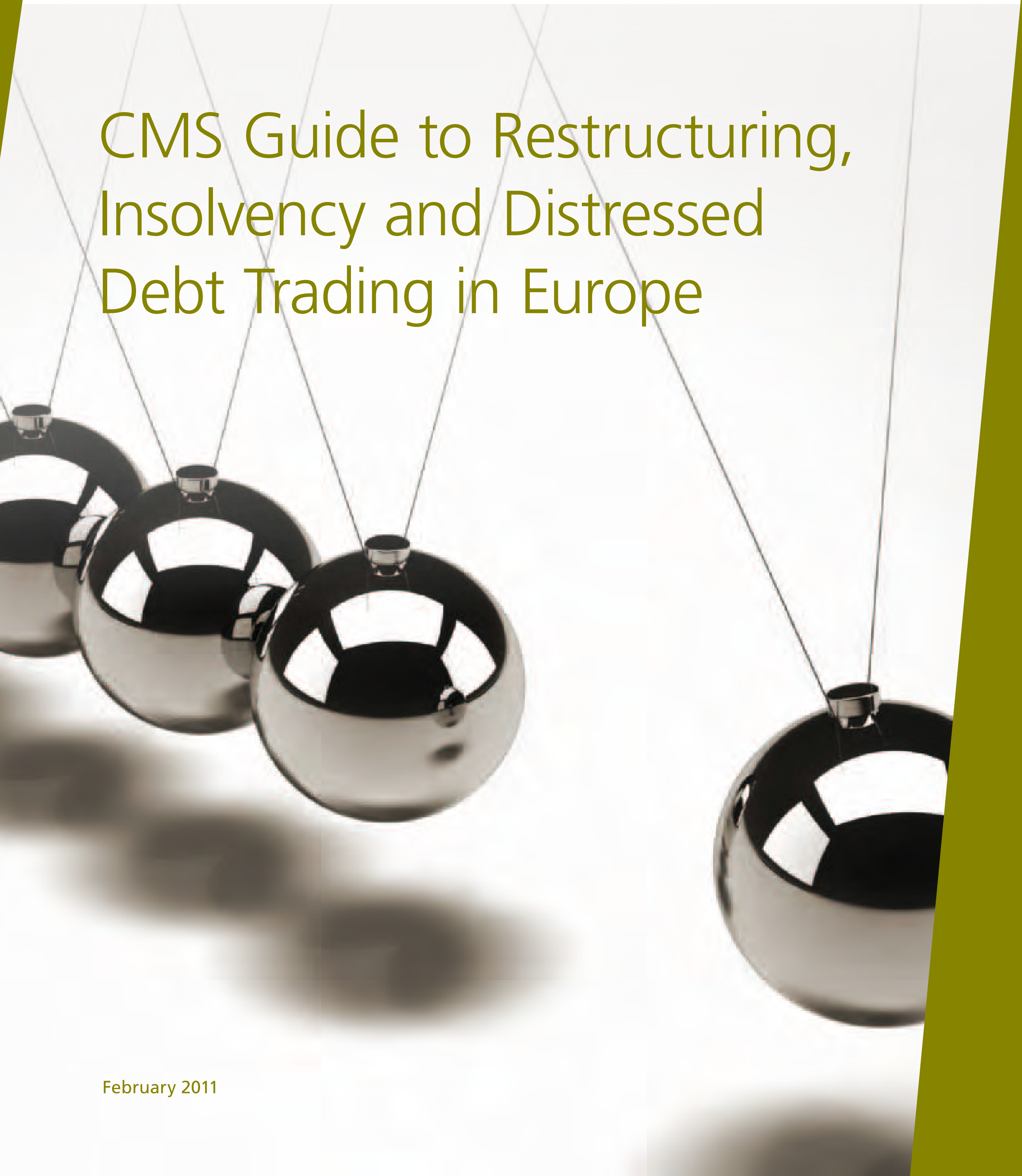
CMS Guide to Restructuring, Insolvency and Distressed Debt Trading in Europe



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Introduction

We are delighted to present the CMS guide to Restructuring, Insolvency and Distressed Debt Trading. This guide provides a comparative analysis of certain key areas of law and procedure for those involved in or affected by financial distress of a corporation and the trading of distressed debt across Europe.

One of the main challenges when dealing with financially distressed businesses with operations in more than one country is that each country has its own unique insolvency and restructuring laws. There is only one piece of pan-EU[1] legislation: the EC Regulation on Insolvency Proceedings[2] , which came into force in May 2002 (referred to in this guide as the "Regulation"). The Regulation recognises the differing laws across the region and the impracticability of attempting to formulate a common code of insolvency law. The Regulation was passed with the relatively modest ambition of codifying an agreement on significant aspects of cross-border insolvencies so that it is easier for insolvency practitioners to deal with cross-border insolvencies.

There is one other piece of international law designed to assist in the area of cross-border insolvency: the UNCITRAL Model Law on cross-border insolvency, which was adopted by the United Nations Commission on International Trade Law in 1997 and has since been implemented into local legislation by several countries including the UK, Poland, Slovenia, Romania, the US and Japan. In the countries where it has been adopted, the UNCITRAL Model Law deals with the recognition of foreign insolvency proceedings and co-operation between courts and competent authorities involved in cases of cross-border insolvency.

We explain the Regulation and the UNCITRAL Model Law in more detail in the first chapter of this guide. The rest of the guide is dedicated to explaining the law and procedure in each jurisdiction on certain key corporate and insolvency and restructuring issues and the law and regulations that govern the sale and purchase of debt on the secondary market. The areas and issues covered, in relation to 20 different European jurisdictions, include the following:

- duties of directors of companies in financial difficulties;
- extending credit facilities to companies in financial difficulties;
- the taking of additional security and/or guarantees in return for bridge finance or other forms of support from lenders;
- options available to lenders for monitoring the performance of companies in financial difficulties;
- debt for equity swaps;
- legal mechanisms available to the majority of a company's creditors to compel the dissenting minority to implement a restructuring plan;
- interaction of formal insolvency procedures and consensual restructuring techniques or sale of the insolvent company's business;

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1 Except for Denmark, which opted out in accordance with Articles 1 and 2 of the Protocol on the position of Denmark annexed to the Treaty on European Union and the Treaty establishing the European Community.

2 Council Regulation (EC) No. 1346/2000 on insolvency proceedings (OJ 2000 L 160/1).

- methods of transfer of non-performing loans and security;
- regulatory issues in respect of distressed debt trading;
- debt buy-backs by the borrower;
- rights of persons who acquire distressed debt to participate and vote in formal insolvency procedures of insolvent companies; and
- impact of data protection and bank secrecy laws on distressed debt trading.

We publish a quarterly newsletter on topical restructuring, insolvency and distressed debt trading issues across Europe. If you would like to receive a copy, please contact:
Elaine Bolwell, Secretary to Martin Brown at CMS Cameron McKenna LLP in London (elaine.bolwell@cms-cmck.com).

If you have any questions arising out of any of the issues contained in this Guide, please do contact us. The main contacts for each jurisdiction can be found on page 122.

CMS Practice Group for Restructuring and Insolvency, February 2011.

About CMS

CMS aims to be the best European provider of high-quality legal and tax advice.

Our detailed knowledge of industries, plus extensive European presence, means that CMS is uniquely qualified to provide highly specialised advice that adds value to your business.

CMS has a common culture and a shared heritage that is distinctively European. With more than 5,000 people working in 53 offices and 28 jurisdictions, CMS has the most extensive footprint in Europe.

Our single organisation of practice groups and sector groups provides clients with high quality advice that is seamless, client-driven and coordinated across borders.

It means we understand your business and can provide the best legal and tax solutions. Our clients expect the best, and we deliver. It is all part of creating and maintaining strong relationships built on trust.

If you are doing business in Europe, or considering such a move, CMS is your best choice for high-quality legal and tax advice.

The CMS Practice Group for Restructuring and Insolvency

Representing all the restructuring and insolvency teams of the various CMS jurisdictions, the restructuring and insolvency practice group has a long history of association and commands strong positions, both locally and on the international market. The group was created in order to meet the growing demand for integrated, multi-jurisdictional legal services in this field.

Members of the Practice Group advise on specialised restructuring and insolvency issues affecting business across Europe.

Restructuring and insolvency issues can be particularly complex and there is a wide range of different laws and regulations affecting them. The integration of our firms across Europe means we can provide coordinated European advice through a single point of contact. Contact details are set out at the end of this guide.

The information contained in this guide is of a general nature and is not intended to be a full legal review of the topics covered and cannot be relied upon for specific advice. We accept no responsibility for any acts or omissions as a result of the information contained in this guide. If you would like to receive specific legal advice, please contact your usual CMS attorney.

The information in this guide is accurate as at February 2011 but please be aware that this is a developing area.

EC Insolvency Regulation and UNCITRAL Model Law

1. The EC Regulation on Insolvency Proceedings

The introduction of the European Regulation on Insolvency Proceedings (Council Regulation 1346/2000) (the "Regulation") in May 2002 was intended to achieve a level of harmonisation in relation to insolvencies across EU Member States (except Denmark which opted not to participate). Given the rise in cross border transactions, the pre-amble to the Regulation outlines the need for coordination of the measures to be taken with regard to an insolvent debtor's assets within the EU.

However, the Regulation also recognises the differing substantive laws across the EU and the impracticality of attempting to formulate a code of insolvency law applicable throughout every Member State. The Regulation therefore only provides rules only on significant aspects of cross border insolvencies. These include which Member State's courts have jurisdiction to open insolvency proceedings, the choice of law applicable to such proceedings, and recognition across the EU of the effects of judgments by a court in a Member State having jurisdiction.

To whom does the Regulation apply?

The Regulation applies to a debtor (who can be either a physical or legal person) having its centre of main interests ("COMI") within a Member State of the EU. Credit institutions and insurance companies are excluded from the scope of the Regulation and are dealt with by separate directives.[3]

Perhaps surprisingly, as COMI is one of the cornerstones of the Regulation, the Regulation itself does not contain a definition of the term. The pre-amble to the Regulation, which serves as an aid to interpretation, but which is not legally binding, provides that COMI "should correspond to the place where the debtor conducts the administration of his interests on a regular basis and is therefore readily ascertainable by third parties". In the case of a company, the place of the registered office is presumed to be the COMI in the absence of proof to the contrary.

The concept of COMI was left to be interpreted by the courts of each Member State, which in some cases has given rise to inconsistencies of interpretation. Also, one unintended consequence of the introduction of the concept of COMI was that a debtor company incorporated outside the EU may fall within the scope of the Regulation if it has its COMI within the EU. This was first shown in relation to a corporation incorporated in Delaware that was put into administration in the UK on the basis that its COMI was in the UK (Re BRAC Rent-a-Car International Inc[4]). The presumption in favour of the place of incorporation or the location of the registered office was rebutted on the facts.

The only case on the interpretation of COMI that has so far been considered by the European Court of Justice is In re Eurofood IFSC Ltd[5]. The ECJ decided that the presumption that COMI is where the registered office is located can be rebutted if factors which are both objective and ascertainable by third parties lead to the conclusion that the COMI is elsewhere. The analysis should focus on where the head office functions of the company are performed, as this will not necessarily coincide with the location of the registered office.

To what proceedings does the Regulation apply?

The Regulation applies to all "collective insolvency proceedings which entail the partial or total divestment of a debtor and the appointment of a liquidator". A "liquidator" is defined as a person whose function it is to administer or liquidate assets of which a debtor has been divested or to supervise the administration of his affairs.

The Regulation defines the terms "insolvency proceedings" and "liquidator" by reference to each Member State in the Annexes to the Regulation.

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3 Directive 2001/24/EC of the European Parliament and of the Council of 4 April 2001 on the reorganisation and winding up of credit institutions (OJ 2001 L125/15) (Council Directive 2001/24/EC) and Directive 2001/17/EC of the European Parliament and of the Council of 19 March 2001 on the reorganisation and winding-up of insurance undertakings (OJ 2001 L110/28) (Council Directive 2001/17/EC).
4 [2003] 2 All ER 201, [2003] 1 WLR 1421
5 [2006] Ch 508

Jurisdiction: main proceedings

Primary jurisdiction is accorded to the courts of the Member State within which the COMI of the debtor is located. Subject to any secondary proceedings (see below) and any relevant exceptions, insolvency proceedings opened in the Member State where the debtor's COMI is located are called "main proceedings" and they are deemed to be of universal scope encompassing all the debtor's assets on a worldwide basis.

Subject only to certain entrenched rights (see below), the law of the Member State in which the proceedings are opened determines the conditions for the opening of those proceedings, their conduct and their closure. Regulation 4(2) lists, not exhaustively, those matters that are governed by the law of that Member State. They include, for example, the respective powers of the debtor and the office-holder, the effects of the insolvency proceedings on current contracts to which the debtor is party and the rules governing the lodging, verification and admission of claims.

Jurisdiction: secondary proceedings

The courts of other Member States have jurisdiction to open secondary insolvency proceedings against a debtor possessing an "establishment" within the territory of that other Member State.

The term establishment is defined as "any place of operations where the debtor carries out a non-transitory economic activity with human means and goods".

Primacy of main proceedings

Secondary proceedings are limited to the assets of the debtor situated in the territory of the Member State in which proceedings are commenced and may only be "winding up proceedings". Various provisions of the Regulation ensure the primacy of the main proceedings, including a requirement on the liquidator of the secondary proceedings to co-operate with the liquidator of the main proceedings.

Recognition

A judgment handed down in the main proceedings will, subject to limited exceptions based on public policy, be recognised and given effect in other Member States with no further formalities.

In addition, the effects of any judgement handed down in secondary proceedings may not be challenged in other Member States.

The liquidator appointed in the main proceedings will be entitled to exercise all the powers conferred on him by the law of the Member State of the main proceedings in another Member State, provided no secondary proceedings have been opened in that other Member State nor any preservation measures to the contrary have been taken there.

Entrenched rights

Certain creditors' rights are excluded from the general choice of law rule in the Regulation and are given entrenched status. Rights in rem (including security rights of a proprietary nature) are one example. So if a debtor has its COMI and main proceedings in, say, France, in general the Regulation dictates that its insolvency and assets (wherever they are) are dealt with according to French insolvency law. But if it also has a creditor with a proprietary claim relating to an asset in, say, Germany, the law applicable to the proprietary claim remains German law. Other entrenched rights include reservation of title claims, set-off and contracts relating to immoveable property.

Problems with the Regulation

The practical application of the Regulation across the Member States since its introduction in 2002 has not always been smooth. There have been instances of 'forum shopping' and jurisdictional conflicts, which the Regulation was supposed to avoid. However, it is hoped that these problems will reduce as the Regulation case law and practice develops. Notwithstanding these early problems, the Regulation represents progress towards co-operation and coordination in the field of international insolvency, for the benefit of insolvent businesses and their creditors.

2. UNCITRAL Model Law on Cross-Border Insolvency (The "Model Law")

The United Nations Commission on International Trade Law (UNCITRAL) (established in 1966) is a subsidiary body of the General Assembly of the United Nations with the general mandate to further the progressive harmonisation and unification of the law of international trade.

Collaboration between UNCITRAL and INSOL International resulted in the adoption in 1997 of the Model Law. The Model Law is designed to assist states to equip their insolvency laws with a modern, harmonized and fair framework to address more effectively instances of cross-border insolvency. Those instances include cases where the insolvent debtor has assets in more than one state or where some of the creditors of the debtor are not from the state where the insolvency proceeding is taking place. The Model Law recognises differences among national procedural laws and does not attempt a substantive harmonisation of insolvency law.

The Model Law has since been adopted by 13 states, including the USA and from the jurisdictions covered by this guide: the United Kingdom (2003), Poland (2003), Romania (2003), Serbia (2004), Slovenia (2007).

The Model Law provides for among other things: foreign assistance for insolvency proceedings taking place in the enacting state; foreign representative's access to courts of the enacting state; recognition of foreign proceedings; cross-border cooperation; and coordination of concurrent proceedings.

In states that have enacted the Model Law, recognition may be sought for foreign proceedings that are collective insolvency proceedings, and which are subject to the supervision and control of a foreign court. The Regulations provide for the recognition of two types of proceedings: foreign main proceedings and foreign non-main proceedings.

Foreign main proceedings

Foreign main proceedings are proceedings taking place in the state in which the debtor has its centre of main interests. As with the Regulation, COMI is not defined but is subject to a rebuttable registered office presumption substantially similar to the presumption in the Regulation. The presumption will be rebutted where there is objective evidence that third parties would ascertain the "head office functions" of the debtor to be in a state other than that of the registered office[6].

Foreign non-main proceedings

Foreign non-main proceedings are proceedings occurring in a state in which the debtor has an "establishment" (which is defined as any place of operations where the debtor carries out an economic activity with human means and goods, which is not of a temporary nature).

Recognition as foreign main proceedings results in an automatic stay of certain types of creditor action including: the commencement of proceedings concerning the debtor's assets, rights, obligations or liabilities; execution against the debtor's assets; and the transfer or disposal of the debtors assets. As with the Regulation, proprietary rights, and set-off are excluded from the general rules.

There is no automatic stay for foreign non-main proceedings, but discretionary relief is available.

6 In the matter of Stanford International Bank Limited and others [2009] EWHC 1441 (Ch)

Austria

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

Directors are not, in normal circumstances, personally liable for the company's debts, but they are under a duty to run the business with the diligence of a prudent businessman. This requires them to maintain a fair overview of the company's financial and economic situation. As soon as they identify a need for reorganisation they are obliged to take appropriate measures, such as convening general meetings, winding up unprofitable parts of the business, obtaining new funds or seeking professional assistance. Failure to comply with their duty to run the business with the diligence of a prudent businessman can lead to the directors being personally liable to the company.

In particular, directors can incur personal liability for any of the following:

— Not filing for insolvency proceedings within the prescribed time limit (see below).

— Not convening a general meeting if the directors knew that the company's net assets (i.e. assets less liabilities) had fallen below the value of half of the company's share capital (taking into account any hidden reserves).

— Not filing for business reorganisation proceedings (*Reorganisationsverfahren*) if:

(i) they received an auditor's report in the two year period before insolvency, stating that the equity ratio (i.e. the ratio of equity to the aggregate of equity and debt) (*Eigenkapitalquote*) was less than 8% and the debt settlement period (*fiktive Schuldentilgungsdauer*) exceeded 15 years; or

(ii) they did not cause financial statements to be prepared and be audited on a timely basis. Reorganisation proceedings are not formal insolvency proceedings, but they provide statutory protection to prevent the company's insolvency.

— Paying or preferring creditors after the point in time when the directors were obliged to file for insolvency.

In certain circumstances, the liability can be criminal, and the directors may also become directly liable to the creditors. Managing directors of joint stock companies and limited liability companies are also obliged to report to the supervisory board without undue delay on all the circumstances that have a material effect on the profit ratio.

Pursuant to the Austrian Insolvency Code (*Insolvenzordnung, the "IO"*), a company is insolvent if:

(i) it is either unable to pay its debts when due (*Zahlungsunfähigkeit*); or

(ii) its liabilities exceed its assets (*Überschuldung*) provided that the company's business continuance forecast (*Fortbestehungsprognose*) is also negative.

Once insolvency has occurred, the company's directors are obliged to file for insolvency proceedings without undue delay, and in any event no later than 60 days after the company has become insolvent.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	A lender considering extending credit facilities to a company in financial difficulties will want to avoid potential liability to other creditors: if the lender extends loans at a time when it is aware that the borrower is insolvent and cannot be rehabilitated, then the lender can be liable for immoral damages for fraud on new creditors or for incitement to delay in filing for insolvency. If a shareholder extends a loan to a company while it is in a financial crisis, the loan may be treated as equity, and the claims under the loan subordinated to other debt obligations of the borrower.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	Transactions occurring less than 60 days before the debtor becomes insolvent or it files for insolvency proceedings that prefer some creditors above others can be challenged by the insolvency administrator. In addition any payments made, or security granted, or other transaction adverse to creditors generally entered into once the company has become insolvent or has filed for insolvency proceedings can be challenged. The aim of these provisions is twofold: first to protect creditors from disadvantageous transactions made by a company in financial difficulties, and second to treat all creditors equally (*par conditio creditorum*). The provisions usually have the effect of preventing a borrower in financial difficulties from granting additional security in respect of existing loans, but a distressed borrower is generally allowed to provide security in respect of a new loan.
4. If a lender wants to monitor the company very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	In practice, lenders do sometimes appoint a managing director to the board of a distressed Austrian borrower. The managing director concerned owes the same duty of care towards the company as any other managing director, and can incur personal liability towards the company in that capacity as outlined in the answer to question 1 above. There are two risks for the lender associated with making such an appointment, or being given extensive approval rights over the management of the company's affairs. First, the lender might inadvertently place itself within the scope of the duty to file for the opening of insolvency proceedings if the conditions are satisfied. This would happen if the lender assumes a management role in relation to the company, or crucial areas of it. The other risk is that the lender might be deemed to be a shareholder, with the effect that the claims under the loan agreement might be subordinated to the claims of other creditors.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Debt for equity conversion is admissible under Austrian law. A debt for equity swap requires a shareholders' resolution to increase the share capital. Such a resolution generally requires the consent of 75% of the shareholders present at the meeting and voting. The debt for equity swap needs to be in the interests of the company so that the subscription rights of the existing shareholders can be excluded. The creditor subscribes for the new shares, and assigns (some or all) its debt claims to the company by way of contribution in kind. The procedure requires an audit of the value of the contributed claims, and an amendment of the articles of association.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	Prior to insolvency proceedings, the debtor may seek to negotiate a consensual, out-of-court settlement (*außergerichtlicher Ausgleich*) with its creditors. This requires unanimous consent of all the creditors involved. There is no formal procedure, but if the debtor is insolvent, it must finalise the settlement within 60 days to avoid having to file for insolvency proceedings. If an out-of-court settlement is not possible, the company commences insolvency proceedings (*Insolvenzverfahren*). According to the Insolvency Code, a company filing for insolvency has a choice of just one insolvency proceeding, but the proceeding covers both bankruptcy (*Konkursverfahren*) (which is terminal and the company is liquidated) and restructuring (which aims to rescue the company). Restructuring proceedings may be initiated if insolvency is merely threatened as well as when the company is actually insolvent. When choosing restructuring proceedings, the company may either use the restructuring plan (*Sanierungsplan*) (which is a rescue procedure supervised by a court appointed insolvency receiver) or the so-called self administration (*Sanierungsverfahren mit Eigenverwaltung*) (which is a debtor-in-possession procedure conducted under the supervision of a court appointed restructuring receiver). When undergoing a restructuring plan, the debtor company must settle at least 20% of its obligations within a period of two years. When undergoing self-administration, the company must settle at least 30% of its obligations within a period of two years. In restructuring proceedings, the debtor must present a restructuring plan, either concurrently with the application for insolvency proceedings or, at the latest, when insolvency proceedings are opened. In a self-administration, the restructuring plan must include detailed information regarding the debtor's assets, and a finance plan showing that (initial) funding has been secured. The restructuring plan must be accepted, and the settlement offer must be approved, by: (i) a simple majority of all creditors present and entitled to vote at the creditors' meeting; and (ii) creditors representing at least 50% of the total amount of all outstanding claims represented in the meeting.
7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	The restructuring proceedings described in the answer to question 6 above enable a company to trade while continuing to pursue a consensual deal with its creditors. If a consensual deal with the creditors cannot be reached and insolvency proceedings have been initiated, the insolvency administrator will usually carry on the business of the company for a period unless or until it is evident that continued trading will increase the loss to the creditors. The insolvency administrator has to realise the assets of the insolvent company in the interests of its creditors and this is often done using a sale of the business as a whole, which enables the business to continue trading under new ownership.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?	Under Austrian law, a lender can assign its rights under a loan agreement. In the absence of contractual provisions to the contrary, the borrower's consent is not required. It is not necessary to notify the borrower, but until the borrower has been notified, the borrower can still validly discharge the debt by paying the assignor. Following assignment, the assignee of the loan assumes the risk of default of the non-performing loan.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	Unless otherwise agreed, the assignment of a claim includes the assignment of ancillary rights (such as security rights).
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Under Austrian law, receivables can generally be freely sold and assigned, unless the parties have agreed otherwise. However, if both the debtor and the assignor are entrepreneurs, an assignment of a loan in breach of a contractual non-assignment clause will be valid and the debtor will only have contractual rights against the assignor for breach of the prohibition on assignment. Creditors may grant a sub-participation under a loan to a third party. A sub-participation does not affect the relationship between the original lender and debtor; it creates an additional legal relationship between the creditor and the sub-participant.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	If the loan transfer is a single, one-off transaction, then it will usually not qualify as a banking activity and therefore no banking licence is required. However, if the loan transfer forms part of a bigger transaction or series of transactions (with a territorial connection with Austria), then the activities may require a banking licence.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	A borrower is permitted to acquire its own debt. If it does so, the debt ceases to exist and is regarded as repaid. A company associated with the borrower may also buy the borrower's debt, but if the borrower is in financial difficulties at the time of acquisition, the buyer's claim may be re-categorised as quasi-equity and be subordinated to the rights of other creditors.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	A creditor who purchases debt after the insolvency proceedings have commenced does not have a right to vote in relation to that claim unless the transfer of debt occurred under a legal relationship created before the declaration of insolvency.

7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Data protection in Austria is governed by the Data Protection Act 2000 (*Bundesgesetz über den Schutz personenbezogener Daten*), which implements the EU Data Protection Directive 95/36 EC. The general view is that bank secrecy provisions do not prevent the assignment of receivables by credit institutions. However, judicial opinion is awaited on certain of the provisions.

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Belgium

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

Directors are under a duty to operate and manage the company at all times in its general corporate interest, namely in the interest of the shareholders, the employees, and the creditors. This general duty is not affected by the company's financial difficulties.

If a company is in financial difficulties, the directors should hold regular board meetings, seek professional advice and maintain regular contact with the company's banks and main creditors.

If the continuity of company is threatened (which is assumed if the net assets of the company fall below half of its share capital (*capital social/maatschappelijk kapitaal*) in the last financial statements), the directors can apply to the competent commercial court for a "judicial reorganisation" (*gerechtelijke reorganisatie/ réorganisation judiciaire*). This procedure is described in more detail in the answer to question 6 below.

If the judicial reorganisation fails, either because the company cannot achieve the reorganisation objectives or because the creditors do not approve the recovery plan, the company can be declared bankrupt (*faillite/faillissement*). The two conditions for a declaration of bankruptcy are a persistent failure in making payments and a considerable deterioration in creditworthiness. The directors are legally obliged to file for bankruptcy within one month of these two conditions being satisfied.
Once the company is declared bankrupt, the bankruptcy trustee (who is appointed by the commercial court) replaces the directors and takes control of the bankrupt company.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	Under Belgian law, a lender can be held liable both towards the company and towards third parties if it has extended (or granted new or additional) credit facilities to a company in financial difficulties, especially where such lender "should have known" that the company was on the verge of bankruptcy. In order to establish lender liability, the company and/or the third party must show that the lender was at fault (in the sense of creating a "false picture" of the company's financial means by extending credit lines), and that this fault caused the party to suffer prejudice as a result of the company's insolvency. If liability is established, the lender can be sentenced by the competent court to reimburse the party that suffered the prejudice, up to the amount of its loss. Arguably, at the same level of knowledge of the financial situation and prospects of the company, lender liability will be triggered the earliest with pure third party creditors, at a later stage with mezzanine financers and only last with shareholders, who have a certain right to attempt to save their company despite certain odds. However, of course, knowledge of the financial situation and prospects of the company (which tends to be inversely proportionate) will also determine lender liability. In short anyone knowledgeable (or who should have been knowledgeable, as a prudent company manager in the same circumstances) of the company's difficulties, will be judged on whether he knew, or should have known, that there was no reasonable chance of recovery.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	Under Belgian law, any additional guarantee or security granted for securing existing debt could be challenged by a subsequently appointed bankruptcy trustee, if it has been granted within a six month period preceding the date when the company is declared bankrupt by the competent commercial court.
4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Under Belgian law, a lender can request that either an observer or a director be appointed to the board of the company. However, a lender cannot unilaterally appoint an observer or a director because such an appointment requires a shareholders' resolution.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	A conversion of all or part of a lender's debt into equity requires the prior authorisation of the company's shareholders to: (i) increase the share capital by an amount equal to the value of the debt being converted (so that new shares can be issued); and (ii) to enable the lender to subscribe for the newly issued shares by means of the contribution in kind of its debt. The transaction also requires an auditors' report, and a board of directors' report. The lender and the company will need to agree a value for the debt being converted and a price for the shares being issued. Debt for equity swaps can give rise to consolidated accounts problems for the lender. If the borrower is a listed company, and the lender is acquiring more than 30% of the share capital of the company, the conversion of debt into equity could result in a mandatory public offer unless the company's equity value is less than 50% of its share capital. It could also give rise to market abuse issues if the lender has privileged information about the company.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	The only such tool available in Belgian law is the judicial reorganisation procedure (*gerechtelijke reorganisatie/réorganisation judiciaire*). The directors can apply to the competent commercial court for a judicial reorganisation if the continuity of the company is threatened (which is assumed if the net assets of the company fall below half its share capital (*capital social/maatschappelijk kapitaal*) in its last financial statements). Creditors of a company cannot initiate a judicial reorganisation (except for a business transfer, as referred to below in the list of objectives that the company or a creditor may apply for during the provisional suspension of payment period). The objective of a judicial reorganisation is to give a company in temporary financial difficulties protection from its creditors while it implements a recovery plan. If the court approves the judicial reorganisation, it will: — appoint a delegated judge (*gedelegeerd rechter/juge délégué*) to supervise the company and keep the court informed of the progress of the recovery plan; and — grant a provisional suspension of payments of six months, which may be extended to twelve months or, in exceptional circumstances, eighteen months. During the provisional suspension of payments the company may apply for the following (which can be applied differently to separate business divisions of the same company): — to negotiate a debt restructuring agreement with two or more creditors; — to hold a creditors' meeting to approve its recovery plan; and/or — to transfer its business, in whole or in part. The court may also order such a transfer in certain circumstances. At the end of the provisional suspension phase, the court will decide whether to grant a definitive suspension, which can last up to a further five years, to facilitate the implementation of the recovery plan. For the court to grant a definitive suspension, a requisite majority of creditors must approve the recovery plan. The recovery plan cannot affect the rights of secured creditors without the creditor's individual consent. At the end of the definitive suspension phase, the court declares the closure of the procedure and discharges the delegated judge.
7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	The judicial reorganisation procedure (see the answer to question 6 above) permits the company to continue its activities while negotiating a consensual deal with its creditors, with a view to either the company's survival or a sale of its business. If a consensual deal cannot be achieved, an orderly sale of the company's assets or business for as much money as possible can be achieved either in a judicial reorganisation (transfer as a going concern) or in a bankruptcy procedure (*faillite/faillissement*). A company in bankruptcy proceedings can continue to trade under the control of the bankruptcy trustee with a view to achieving a sale of the company's business and assets, but trading in bankruptcy is not always possible, especially if the bankruptcy trustee needs to exercise his powers to terminate some or all the company's contracts.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?	Under Belgian law, a non-performing loan can be transferred by way of assignment. The borrower must be notified. No specific formality is required for such a notification. The assignor remains liable for any remaining lender obligations under the loan unless released by the borrower. Transfer by novation should be avoided under Belgian law, because it can have the effect of automatically releasing any corresponding security. The parties may however contractually decide that certain security should survive, including a mortgage and a legal lien (*privileges légaux/wettelijke voorrechten*). There is a debate under Belgian law as to whether such a decision of the parties can also apply to other types of security, for example the pledge agreement.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	In case of an assignment, any collateral is automatically transferred. However a pledge over the whole business and assets of a company (which takes the form of a floating charge) can only be granted in favour of certain "qualified" lenders. As a consequence, if the loan being transferred is secured by such a pledge and the assignee of the loan is not a "qualified" lender, it should be considered separately as to how equivalent security could be granted. For the position in relation to a novation, please see the answer to question 1 above.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under English law?	Sub-participation agreements are permitted under Belgian law. Sub-participation is the transfer of an existing lender's (Party A) economic risk associated with the debtor to a new lender, the participant (Party B). Under the terms of the sub-participation agreement, Party A remains the legal holder of the claim and accordingly the 'lender of record', so far as the debtor is concerned. This means that Party A remains liable to the debtor for any undrawn commitments under the facility agreement. In turn, Party B agrees to reimburse Party A in respect of any amounts that Party A is required to advance to the debtor under the facility agreement. Additionally, Party A will agree to pass all receipts (namely principal, interest and other monies) that are referable to the participated tranche to Party B, as and when they are received from the debtor. Party A will also (depending on whether or not this is included in the sub-participation agreement), act on the instructions of Party B in relation to issues such as voting. Unless there is a prohibition in the original loan agreement (which is unlikely), sub-participation can be effected without the consent of, or disclosure to, the debtor.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignee or the borrower?	Belgian regulatory law does not generally require a licence or prior authorisation for the purchase, sale and/or transfer of a non-performing loan. However, as noted in the answer to question 2 above, if the loan is secured by a pledge over the whole business and assets of the company by way of a floating charge, the security can only be transferred to a licensed credit institution or a financial company. Purchase, sale and/or transfer of a non-performing loan would not qualify as the provision of banking/financial services in Belgium.

5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	Belgian law does not prohibit a borrower (or a company associated with the borrower) from buying debt that it owes to a lender.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	In the case of judicial reorganisation, any purchaser of a claim against the insolvent debtor during the course of the insolvency process also takes the voting right in relation to the acquired claim. In the case of bankruptcy procedure, there is no provision for creditor voting and therefore no vote to transfer to the acquiring party.
7. Are there any data protection or confidentiality issues in your jurisdiction that would hinder or prevent a lender from selling and/or transferring loans?	Belgian data protection laws prohibit disclosure of personal data without the subject's consent. Such consent is usually given in the facility agreement by means of a confidentiality clause, which sets out the circumstances in which the lender is entitled to disclose information received from, or in respect of, the debtor to a third party. For a standard LMA facility agreement this will normally include the right to pass this information to a potential purchaser of the loan, provided that the purchaser is either (i) an existing lender or (ii) a potential purchaser of the loan (and that in the case of (i) the potential purchaser has entered into the LMA standard form confidentiality agreement). If there are no provisions in the facility agreement that allow information to be passed to a potential purchaser then the consent of the debtor may be required in order to do so, so care must be taken in order to avoid breaching the lender's duty of confidentiality. Parties also need to ensure that information received in relation to companies or groups whose securities are traded on certain public markets is handled appropriately. For instance, information received in relation to a company's banking arrangements may be "private" and/or potentially price-sensitive, which may prevent that party from trading in the public securities of that company and/or its affiliated parties.

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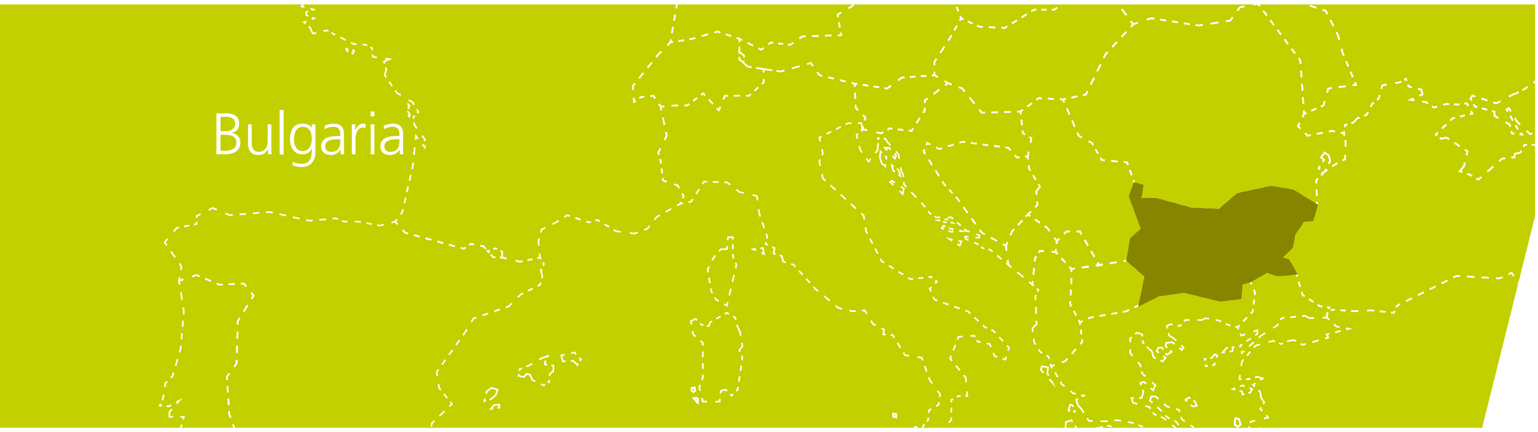
Bulgaria



FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

In Bulgaria, insolvency is defined both by reference to an inability to pay debts when due and over-indebtedness, where a company's assets are insufficient to cover liabilities. Directors of an insolvent company are obliged to file for the opening of insolvency proceedings within 30 days of insolvency occurring, and the procurator is obliged to notify traders that insolvency has occurred within 7 days.

Failure to comply with this 30-day deadline can result in personal liability to the company's creditors for damages caused by the delay, and even criminal liability including a fine or imprisonment.

In addition to the obligation to file for insolvency, directors of a limited liability company are also obliged to convene a general meeting of its shareholders immediately if the company has suffered losses that exceed a quarter of the registered capital of the company. Failure to do so can result in personal liability to the company for any damages caused and the shareholders can initiate legal proceedings against the director or controller on behalf of the company.

Similar rules also apply to the directors of a joint stock company:

- (i) each of the executive directors must inform the chairman of the board immediately of any circumstances that are material to the company; and
- (ii) in the event that losses exceed one half of the company's share capital, the board is obliged to convene a general meeting within 3 months. Failure to comply can result in personal liability for damages caused to the company.

A director may request a release from liability (except for criminal liability) from the general meeting of shareholders, which can adopt a decision to that effect. The release of liability could be for a particular case or for a certain period of time of performance of its duties (if the director has not caused damages to the company intentionally or negligently).

If a company is experiencing financial difficulties the board of directors should closely monitor the company's financial position and seek advice.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?

There are no express restrictions on creditors extending credit facilities to a company in financial difficulties. If the lender advances funds to a company in financial difficulties or if an insolvent company takes a new loan, the directors of the company who approved the transaction may be liable if they acted against their company's interest.

Any loan advanced after the date of the commencement of insolvency proceedings is paid on its maturity date. If there are insufficient funds to pay the loan in full on its maturity date, the lender's claim ranks in priority to unsecured creditors.

Shareholders' loans (whether granted before or after the opening of insolvency proceedings) rank in priority behind all other creditors (Article 616, Paragraph 2 of the CA).

3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?

Any security granted after either the commencement of insolvency proceedings or, if earlier the date on which the court determines that insolvency occurred, is null and void as against the company's creditors. Furthermore, Bulgarian legislation provides that certain transactions entered into during "suspect periods" can be challenged and can become null and void in law or can be revoked. They can be summarised as follows:

(a) gratuitous transactions (except for ordinary gifts) entered into two years prior to the commencement of bankruptcy proceedings;
(b) undervalue transactions, entered into within two years prior to the commencement of bankruptcy proceedings;
(c) repayment of monetary obligations by the transfer of property, within three months prior to the initial date of insolvency;
(d) the grant of security to secure a previously unsecured claim within one year prior to the commencement of bankruptcy proceedings; or if the security was created in respect of the claim of a shareholder, the period is two years; or
(e) a transaction effected within two years prior to the commencement of bankruptcy proceedings that prejudices creditors' rights, if a party related to the debtor is party to that transaction. Related parties include: spouses or close relatives; employers and employees; persons, one of whom participates in the management of the other's company; shareholders; a company and a person who holds at least five per cent of voting shares in the company.

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?

If provided for in the facility agreement, a lender may nominate a person to be a member of either the supervisory board or the management board. The shareholders in a general meeting or the supervisory board respectively must approve the appointment. The lender appointee would be subject to the same duties and obligations as any other supervisory or management board member (please see the answer to question 1 above). Alternatively, the lender may ask an observer to be appointed on the board(s), who would have the right only to observe the respective body's meetings but not to vote, or it could request the regular provision of information such as the agenda of board meetings; the minutes of the meetings, etc.

5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Under Bulgarian law, a debt for equity swap can be done using either an in-kind contribution procedure, or a recovery plan. The procedure for swapping debt for equity using an in-kind contribution requires: (a) a shareholders' resolution in a general meeting to approve the debt for equity swap; (b) an assessment by three independent experts of the value of the debt being exchanged. The nominal value of the shares subscribed for cannot be higher than the value of the debt; and (c) the name of the lender/contributor and a detailed description of the in-kind contribution to be added to the articles of association. Where a debt for equity exchange is being performed as part of a recovery plan, it must include: (a) a list of the names of lenders who have agreed to swap debt for equity; (b) a full description of in-kind contributions; (c) their cash value; (d) the grounds of the lender's rights; and (e) the number, the type and nominal value of the stakes or shares, that are being acquired. A court decision approving the recovery plan is necessary and it has the same effect as a decision by the shareholders in a general meeting to increase capital by way of an in-kind contribution. The Bulgarian Credit Institutions Act limits the proportion of a bank's own capital that can be invested in qualifying equities and also the maximum size of equity stake a bank can hold in any single entity. Therefore, if the lender wishing to swap debt for equity is a bank, its resulting equity participation must not exceed the statutory requirements.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	After insolvency proceedings have been opened, a recovery plan can be proposed by a number of different stakeholders, including: the debtor; the insolvency receiver; creditors holding at least a third of the secured claims, or alternatively a third of the unsecured claims; shareholders holding at least a third of the company's share capital, or shareholders with unlimited liability; or 20% of the employees. Rules dictate the form and content of the recovery plan and creditors voting in five separate class meetings must approve it. The plan is adopted if a simple majority of the amount of the claims within each class of creditors accept it, and the court subsequently approves it. The court will approve the recovery plan only if it provides that dissenting creditors will receive what they would have received if the company was liquidated instead of entering into a recovery plan. Once approved, the recovery plan is binding on all creditors of the company whose claims have existed since before the opening of insolvency proceedings. Apart from the recovery plan described above, there is no other (pre-insolvency) mechanism in Bulgarian law to compel a minority of dissenting creditors to agree to a debt restructuring.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either:
(a) a consensual deal with creditors that will see the company itself survive; or
(b) an orderly sale of the company's assets/business?

The only formal statutory procedures available to a company in financial difficulties to achieve either a consensual deal with creditors to secure the company's survival, or an orderly sale of the company's assets or business exist within insolvency proceedings. After commencement of the insolvency proceedings the company continues to perform its activities under the supervision of an insolvency administrator (*"syndic"*). The company may conclude new transactions only with the prior consent of the insolvency administrator.

A consensual deal with creditors to secure the company's survival can be achieved using an out-of-court settlement. The out-of-court settlement must be in writing and must follow a certain statutory form for it to be legally binding. It must be agreed by the debtor and all the creditors, and approved by the court. If the executed settlement complies with legal requirements and there are no disputes relating to the claims of the creditors, following its approval by the court, the competent court will then adopt a decision to terminate the insolvency proceedings. If the debtor fails to meet its obligations under the out-of-court settlement, insolvency proceedings can be re-opened.

If the creditors' unanimous consent cannot be achieved, the debtor can use a debt recovery plan (please see the answer to question 6 above). The court's decision approving the recovery plan terminates the insolvency proceedings. However if the debtor does not comply with the recovery plan, the creditors holding at least 15% of the aggregate amount of the claims or the supervisory body (which could be appointed to exercise control over the debtor's activity during the period when the recovery plan is in effect or for a shorter time period), may request a re-opening of the insolvency proceedings.

Alternatively, a recovery plan can provide for the sale of part or all of the company's business by attaching a draft agreement signed by the prospective buyer to the recovery plan itself. If none of these options are possible, the receiver can, in accordance with the decision of a meeting of creditors, offer for sale some or all the company's assets. A sale of assets must also be approved by the court.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?

Under Bulgarian Law, loans can be transferred either by assignment or by novation. However, assignment cannot be used to transfer both rights and obligations together, in the same agreement.

(a) Assignment is the most common method of loan transfer, and it occurs in the form of an assignment of rights/receivables and an assignment of obligations:
An assignment of receivables (cession agreement) is used to transfer receivables under a loan agreement. The lender can remain as an obligor to the borrower in respect of any outstanding obligations or it can assign the obligations separately (please see below). If the loan is secured by a mortgage, a notary must authenticate the parties' signatures to the assignment agreement. To be enforceable, the borrower must be notified (but need not consent). The assignor/lender is not liable to the assignee (new lender) for the debtor's default unless agreed otherwise. Substitution in debt operates to assign the lender's obligations. Under this process, a new lender agrees to replace the existing lender in respect of the outstanding obligations under a loan agreement, provided that the borrower's consent is obtained (otherwise the out-going lender cannot be released from liability). This method is not the same as novation, where the receivables/obligations are discharged and replaced by new receivables/ obligations (please see below). Step-in debt is used where it is not practical to obtain the borrower's consent for the substitution in debt.

	The most common use of step-in debt is where the original lender and the new lender agree to be jointly liable for the outstanding obligations towards the borrower. As previously mentioned, the borrower's consent is not required, but if consent is given, the original lender will be substituted by the new lender. (b) Novation is an alternative to assignment when there is a change of the lender and the terms of the loan are being varied. Novation takes effect by discharging the original rights and obligations and replacing them with new ones. A novation requires a multilateral agreement (between the original lender, the new lender and the borrower) because the borrower's consent is needed, and if a mortgage has been used as collateral, a notary must authenticate the signatures of the parties to the novation agreement.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	Where the receivables under a secured loan have been assigned, the related security generally transfers automatically. Where the relevant security is registered, the assignment must also be registered with the relevant registry to enable the new lender to enforce it. Where the assignment is a substitution of the borrower by a new debtor and the security has been provided by a third party, the security will be transferred only with the consent of the security provider. In the event of novation, any related security is terminated unless the novation agreement provides for the existing security to be transferred to the novated loan, and the security provider consents. Please note that generally speaking Bulgarian law does not recognise security agents or security trustees. An explicit exception to this is made for the financial collateral arrangements with respect to the bondholders' agent in a bond issue.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Sub-participation is permitted but not specifically recognised under Bulgarian law. It is infrequently used and is usually limited to loan trading within the same group of companies because it exposes sub-participants to certain risks. Sub-participation is effected by an agreement between the existing lender and the sub-participant whereby they share both the risks and benefit of their respective portion of the loan agreement. There is no formal transfer of the receivables and no corresponding automatic transfer of any collateral. Bulgarian law does not differentiate between legal and beneficial title to ownership, nor does it recognise rights held on trust. Therefore, the sub-participant's interest in the loan is not recognised in law. Sub-participants will sometimes negotiate the right to have security transferred and registered in their name by way of an assignment upon the occurrence of certain events (such as an event of default), but this can add cost.

4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	Under Bulgarian law, a banking licence is not generally required to engage in lending activities if the funding for such loans is not sourced through the public solicitation of deposits. However, granting and/or purchasing loans with a lender's own funds does fall within the scope of providing financial services. If carried on regularly and as a main activity, the loan provider/buyer, although not requiring a banking licence, will fall within the definition of a financial institution and, although it may not require a banking licence, it must register with the Bulgarian National Bank, and also must comply with the statutory requirements for a financial institution. In addition, details of financial loans (defined as all loans, excluding commercial loans) between Bulgarian and foreign persons must be provided to the Bulgarian National Bank for statistical purposes.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	Bulgarian law permits a borrower (or a company associated with the borrower) to buy debt that it owes to a lender. The purchase of its own debt would be treated as payment of the borrower's obligations. As a principle of contractual freedom, the borrower may also agree with the lender to buy its own debt at a reduced price.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	For any creditor to have the right to vote on its claim in insolvency proceedings, the claim must have been filed at court within one month (occasionally three months) from the date insolvency proceedings were opened and registered with the commercial registry. If the claim has not been filed and the statutory deadline has not passed, the acquirer of the claim can file it. Provided the claim has been filed at court, the purchaser of the claim or debt may step into the rights of the original creditor only with the consent of both of the original parties.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Bulgarian bank secrecy laws and data protection laws prohibit disclosure of bank secrets and personal data without the subject's consent. It is therefore usual practice to include in the original loan agreement the borrower's prior consent to disclosure for the purposes of loan trading.

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Croatia

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?	Under Croatian law, directors are not, in normal circumstances, personally liable for the company's debts, but they are under a duty to run the business with the diligence of a prudent businessman. As soon as the directors learn of any material change in the company's financial reports and, in particular, if the company suffers a financial loss equal to half or more of the nominal value of the company's share capital, the board of directors must immediately convene a general meeting. If a company becomes insolvent (which occurs under Croatian law if it has been unable to pay its debts for 60 or more days, or its current obligations exceed its existing funds), the directors are obliged to initiate insolvency proceedings within 21 days. Also once the company is insolvent, the directors must ensure that it does not make any further payments, except after carrying out due diligence to the standard of a prudent businessman. Failure to comply with these duties can result in the directors becoming liable to compensate the company for any loss caused, and in some cases can result in a criminal fine or even imprisonment for up to two years. If directors act in accordance with the general meeting's decision, they will not be liable for any loss that may be suffered, but a supervisory board's approval does not absolve a director from liability. Once a company experiences financial difficulties, and before any obligation to initiate insolvency proceedings has occurred, the directors can minimise their personal exposure by ensuring they have up to date financial information and by seeking professional advice.
2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	Creditors can extend credit facilities to a company in financial difficulties and in theory it can be for an indefinite term. However, if an insolvency procedure is initiated, all undue claims immediately become due.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	Granting new security in such circumstances (specifically in the three month period before the initiation of insolvency proceedings) may render the transaction vulnerable to challenge by a subsequently appointed liquidator pursuant to the Insolvency Act (Official Gazette No 44/96 as amended). This provision also applies to any transaction related to the granting of the offending security. When a company is in financial difficulties, if the directors dispose of any of the company's assets, or make any payments that a prudent businessman would not dispose of, or make (respectively) in those circumstances, the directors can be held liable for any damages caused (please see answer to question 1 above) and the transaction may be declared null and void.

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Unless otherwise agreed with the company in the credit agreement, there is no formal mechanism that allows a creditor to monitor the company more closely in this way. However, in practice the company can allow the creditor (for example its bank) to appoint someone to observe board meetings.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company, and what consents are required?	A debt for equity swap is possible under Croatian law. In the case of both a limited liability company (*d.o.o.*) and a joint stock company (*d.d.*), a lender's debt can be used as consideration for new shares in the company. A joint stock company also has the option to issue a convertible bond to a lender, which can then be exchanged for shares in the company by way of a conditional share capital increase. In both cases, a prior audit must be performed by the court-appointed auditor to establish or verify the values attributed to the debt and the equity being swapped. It is also possible to perform a debt for equity swap where the debt is a loan given by an affiliated company, and it is transferred into the capital reserves of the company. However this particular type of debt for equity swap can only be done if the company's articles of association expressly allow it. It does not require an audit.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	Outside of insolvency proceedings, there is no formal mechanism that enables the majority creditors to compel minority creditors to agree to a restructuring plan. Any such pre-insolvency agreement can only be done informally and only with the consent of all creditors. Once insolvency proceedings are initiated, the creditors' assembly can mandate the bankruptcy trustee to create a reorganisation plan (*stečajni plan*), which determines how the company's debt will be restructured, with the intention of securing the company's survival and avoiding a liquidation procedure. A reorganisation plan can propose a wide range of solutions including: debt reduction, debt for equity swap, a financial or equity restructuring, and the sale of some or all the company's business or assets. The creditors' assembly is the body that represents all creditors throughout the insolvency proceedings, and it has the right to decide (subject to the court's confirmation) the future of the company's business activities and the terms of settlement of any debts. Acceptance of the reorganisation plan requires a two-thirds majority (in value) of the creditors who vote at the creditors' assembly. If both the creditors and the company accept the reorganisation plan, the court decides whether to confirm it. If accepted by creditors and approved by the court, the reorganisation plan is binding on all creditors. Unless the reorganisation plan determines differently, claims of lower-ranking creditors (including, for example penalty interest that accrued on creditors' claims during the insolvency proceedings) cease to exist. If the creditors' assembly rejects the reorganisation plan, the company is liquidated.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	There are no such formal statutory procedures outside of insolvency proceedings. Under insolvency law in Croatia a company can be either reorganised or liquidated. During insolvency proceedings, the company can, both before and after the decision whether to reorganise or liquidate is taken, continue to trade under the supervision of the bankruptcy trustee if the creditors' assembly so decides. The decision of the creditors' assembly to continue trading requires a simple majority (in value) of those creditors present and voting at the creditors meeting. In practice such trading is usually reduced to the minimum activity necessary to preserve the company's business while a reorganisation is progressed. Reorganisation as a procedure is intended to achieve the survival of the company and/or its business. As mentioned in the previous answer, it can involve either a debt restructuring (which can be either consensual or crammed-down, see the previous answer) or an orderly sale of the company's business. Liquidation can involve an orderly sale of the company's assets or business, but will ultimately result in the liquidation and distribution of the company's assets and the dissolution of the company.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?	A lender can transfer a non-performing loan by way of assignment. In general, the debtor does not need to consent to the assignment, but it must be notified. The exception to this is if the debtor and lender have agreed that the debtor's prior consent to an assignment is required, in which case an assignment of debt without consent is null and void.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	When a non-performing loan is assigned, any related security is automatically included in the loan transfer. However, formal steps have to be taken in order to notify the competent registries regarding the change of beneficiary.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	The laws and regulations of Croatia are silent on sub-participation agreements and, even though they are not prohibited, they are not common in practice.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	Only financial institutions and banks that are licensed by the Croatian National Bank (*"CNB"*) can provide regulated banking and financial services. The provision of loans usually falls within this definition and therefore a CNB license is required. However, no additional licence or prior authorisation is required for the purchase, sale and/or transfer of non-performing loans. If the lender is an affiliated foreign company of the debtor, no additional licence from the CNB is necessary. However under certain conditions, the loan transfer transaction has to be registered with the CNB and the capitalization rules have to be respected.

5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	A borrower (or a company associated with the borrower) is permitted to buy debt that it owes to a lender(s), provided that all banking and financial regulations are complied with.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	Once the claim is assigned, the assignee creditor is entitled to exercise all the rights that the assignor creditor had (including the right to vote), and is bound by all the corresponding obligations.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Data exchange in relation to a prospective loan transfer is allowed provided (i) the original loan agreement permits exchange of data; (ii) data protection rules are complied with; and (iii) bank secrecy laws are obeyed. Among other things, bank secrecy laws prescribe the mode and volume of transfer and processing of data that banks acquire from clients in the daily course of business. Banks are obliged to protect such data, which can only be disclosed or distributed as prescribed by law. Examples of permitted disclosure include disclosure required by tax authorities, or by court order for the purposes of court proceedings, or with the prior consent of the client.

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Czech Republic

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

As a general rule, directors have a duty to act with the care of a prudent businessman, which requires among other things an awareness of the company's financial statements and its financial condition. Failure to comply with this obligation could result in the directors being held liable for consequential loss caused to the company, or even criminal liability.

Directors of a limited liability company (executive directors) or a joint stock company (members of the board of directors) are obliged to call an extraordinary general meeting of the company's shareholders if

- (i) the unpaid part of the company's losses amounts to at least one half of the company's registered capital or
- (ii) the company is insolvent.

At the meeting, the directors should propose either that the company be dissolved or that alternative measures be adopted. In this context, the term "losses" means the sum of the unpaid losses from previous years in the company's profit and loss account and the established loss for the current financial year as set out in the company's financial statements, approved by the ordinary general meeting.

Czech law does not define the term "financial difficulties". Statutory provisions only define insolvency (and impending insolvency) as something amounting to a more serious stage of financial difficulty. Insolvency in Czech law occurs if:

- (i) the company is unable to pay its debts within 30 days of their due date. A company is deemed unable to pay its debts if:
  - (a) it ceases to pay a substantial part of its debts; or
  - (b) it is in default for more than three months; or
  - (c) a creditor's attempts to satisfy its claims by means of court enforcement or execution against the company are unsuccessful; and/or
- (ii) the company is over-indebted in the sense that it is balance sheet insolvent.

If a company becomes insolvent, the directors must file an application without unnecessary delay to commence formal insolvency proceedings with the competent court. Failure to comply with this obligation will result in the directors being liable for any consequential damage caused to the company's creditors. In addition, such failure could also result in criminal liability.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	If the company is in financial difficulties, its creditors must carefully consider how serious such difficulties are and whether there is a risk that the company has already become insolvent. However, Czech law does not contain any provisions imposing liability for over-extending loans and creating a false impression of liquidity. Directors can incur criminal liability if during the negotiations preceding the execution of a credit facility agreement they make a material misrepresentation or they conceal material circumstances (including that the company is insolvent). If insolvency proceedings have been commenced, the insolvency administrator may enter into loan facility agreements (or similar agreements) and related security agreements on behalf of the company on market terms in order to keep the company operating. The company's existing secured creditors have a right of first refusal to enter into such agreements with the insolvency administrator, provided that the terms they offer are no less favourable than the best terms offered by a third party.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	In the course of the insolvency proceedings, the insolvency administrator can enter into loan agreements and security agreements with the insolvent company's financial creditors in certain cases (see question 2 above). If an insolvent company enters into a new security document within the one year period before formal insolvency proceedings start, or three years if the security is granted in favour of an affiliate of the company or a "close person" (which includes directors and shareholders), and if the purpose of the security is to secure the company's existing obligation by encumbering the company's assets or property, such a security agreement is considered a preferential transaction. A preferential transaction is defined as a transaction that promotes one creditor's debt at the expense of other creditors in the event of subsequent insolvency. The insolvency court can set aside such an agreement if challenged by the insolvency administrator.
4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Before the company has entered into insolvency proceedings, the lender can only monitor the company in accordance with the provisions of the facility agreement. Theoretically, the shareholders could appoint a director or observer to the board, who could be a person nominated by the lenders. However such an appointment would be unusual, and it would probably also require an amendment to the company's constitution. Moreover, the extent of possible lender's monitoring of and influence on the company in such cases should be considered carefully. According to a recent court decision, if the financing documentation enables the lender to monitor the company's financial position closely and to have certain rights vis-à-vis the company's management, there is risk that the courts would consider the company to be dependant on the lender to such an extent that both these entities have created a concern. This may result in the limitation of certain of the lender's rights, e.g. the lender may be excluded as a member of the creditors' committee in the insolvency proceedings (which does not affect the lender's registered claims directly, but may affect the lender's ability to influence the insolvency proceedings). Although this decision has not been widely accepted by Czech lawyers, it is advisable that it is considered when preparing the financing documentation. During insolvency proceedings (which can include a formal reorganisation), lenders can monitor the company more closely by becoming a member of the creditors' committee. See the answer to Question 7.

5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	There is no express statutory provision under Czech law regulating the right of lenders to exchange their debt for equity. Such a process might be possible on a contractual basis pursuant to an agreement between the shareholders and the lender, although certain regulatory restrictions must be complied with. Czech law restricts banks from acquiring equity in other entities (which are neither banks nor other financial institutions). A bank may not exercise 'control' over such an entity. Furthermore, a bank cannot invest more than 15% of its capital in a qualifying holding in any one single company, and in addition it cannot have more than 60% of its capital invested in qualifying holdings generally (as opposed to other types of investments). A qualifying holding is a direct or indirect holding that either represents 10% or more of the capital or the voting rights of a company or that enables the bank to exercise a significant influence over the management of the company. The above restriction is relaxed where the relevant shareholding held by the bank is held during either a rescue period or the financial reconstruction of the company and where such shareholding is held for no longer than three years from the date of acquiring it. Subject to the above restrictions, a lender with security over shares in a limited liability company can, by way of enforcing the security, acquire the shares over which it holds security if it does not first succeed in enforcing the security and selling the ownership interest at a public auction. A lender may exercise rights related to pledged shares in a joint stock company and dispose of them, provided that security is created in the form of financial collateral and the lender's rights were agreed between the parties. In this case, the lender does not exchange its debt for the company's equity directly, but its position resembles that of a shareholder in certain respects. Creditors of an insolvent company can also become shareholders of a new company that has been formed as part of a reorganisation to acquire the business and assets of the old company.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	There are no mechanisms expressly regulated by Czech law, other than formal insolvency proceedings, that enable majority creditors to cram down a restructuring plan on a dissenting creditor minority. Restructuring, in the form of a formal reorganisation, is expressly regulated by law as one of the methods of resolving insolvency, see question 7 for a brief description of the formal reorganisation procedure.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?

The only formal statutory procedures available to a company in financial difficulties are formal insolvency procedures. Following the commencement of insolvency proceedings, either: (a) reorganisation (*reorganizace*) can be used as a method of restructuring the company in an attempt to ensure its survival; or (b) the bankruptcy provisions (*konkurs*) apply, which lead to liquidation of the company.

Generally, reorganisation applies to companies with a total aggregate turnover in the financial year before the insolvency proceedings were initiated of at least CZK 100,000,000, or those with at least 100 employees.

Reorganisation of "smaller" entities is also possible provided the debtor submits a reorganisation plan to the insolvency court that has been approved by at least 50% (in value) of

(i) the secured creditors and
(ii) the unsecured creditors either with the insolvency petition, or no later than 15 days after the court's decision on insolvency is issued.

Reorganisation is not admissible for debtors in liquidation, securities and commodities exchange brokers and traders.

The main purpose of reorganisation is to solve the existing or threatened bankruptcy of the debtor while maintaining the debtor's enterprise.

A petition for reorganisation may be filed either by the debtor or by the creditor. The reorganisation proposal must be approved by a majority (in value) of creditors present and voting at the creditors' meeting (divided into creditor groups) and subsequently approved by the court. The creditors' meeting also elects a creditors' committee (if there are more than 50 creditors) or a representative (if fewer than 50). The creditors' committee or representative has powers to supervise the insolvency administrator during the insolvency process.

The reorganisation itself is executed pursuant to a reorganisation plan, which is put together by the company (even if the reorganisation is initiated by a creditor). The company has to present the plan to court for approval within 120 days of the decision to allow the reorganisation, but this period can be extended by another 120 days under certain conditions. Creditor groups must again vote in favour of the reorganisation plan, but the court does have power to approve the plan even if it has not been accepted by all creditor groups, provided at least one creditor group has approved it and it is fair to objecting creditor groups.

After the reorganisation plan has been submitted and approved, the debtor continues to manage its assets and conduct its business activities, supervised by the court-appointed insolvency administrator and under the control of the creditors' committee (or representative as appropriate) whose approval is required to dispose of any material assets. The insolvency administrator also exercises the powers of the debtor's general meeting. However, the right of the debtor at the General Meeting or shareholders' meeting to appoint or elect or remove members of the debtor's mandatory body and Supervisory Board, if approved by the creditors' committee, survives. The Insolvency Act also provides for certain increased responsibilities of the debtor's statutory body, for example they, along with the debtor, will be construed as guarantors for any damage caused by the debtor during the reorganisation process.

DISTRESSED DEBT TRADING	
1. How does a lender sell a loan?	A lender can, in most cases, "sell" a non-performing loan by way of assignment. The old lender assigns its receivables arising under the loan agreement using an assignment agreement entered into between the old lender and the new lender. The original loan agreement stays in place and the assignment, in terms of its effect on the debtor, is effective from the moment the debtor receives notification of the assignment.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	Yes. Any security interests related to the assigned receivables are included automatically in the assignment. The consent of the security provider is not required. The assigned receivables remain in the same condition as they were prior to the assignment. The Civil Code imposes an obligation on the assignor (i.e. the original lender) to notify the persons providing security of the assignment, although there are no direct sanctions where this obligation is breached.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Czech law does not recognise sub-participation or the distinction between the lender of record and the participant in such a case. However, loan agreements governed by Czech law usually contain a provision under which the lender has a right to assign its receivables to a third party.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	The purchase, sale and/or transfer of non-performing loans are not listed as banking services that require a licence from the Czech National Bank, which is the relevant licensing authority for banking and financial services. An entity incorporated in the Czech Republic whose business activity is the sale, purchase and/or transfer of non-performing loans can operate its business on the basis of a general trading licence.

5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	Theoretically, a borrower can buy debt that it owes to a lender, in which case the loan (or part of it as the case may be) would cease to exist by operation of law as a result of the consolidation of the position of the debtor. Such an agreement might also be considered a settlement agreement between the lender and the borrower (in the event that the purpose of such a transaction is to replace the existing rights and obligations with new ones). A company associated with the borrower may buy the borrower's debt, although such a transaction may be caught by related party transactions provisions. A related party transaction occurs when a company enters into a loan or credit agreement with a member of its board, procurator or another person authorised to act in the name of the company, or with persons close to them, or a contract to secure the obligations of these persons, or a contract to transfer company property to any such person for no consideration. A related party transaction requires the prior approval of the general meeting, and must be made on ordinary business terms. Further, if the company acquires or transfers assets from or to its founder shareholders, or persons acting together with them, or related persons (such as members of board, supervisory board, affiliated persons) or persons acting together with them, and the consideration for such assets exceeds (or is likely to exceed) one tenth of the registered capital of the company, the value of the transferred assets must be assessed by an expert valuer appointed by the court.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	A party acquiring a claim against an insolvent debtor by way of assignment after the commencement of insolvency proceedings would assume the position of the original creditor (including taking over its voting rights) as its successor in the insolvency proceedings, once the accession has been approved by the insolvency court.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Generally, information about a loan is protected by secrecy provisions in the Act on Banks, and it cannot be disclosed without the borrower's consent. Czech banks usually include provisions in their general terms and conditions that give them the right to assign a loan, and provide the assignee with the relevant information about the loan and the borrower.

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England, Wales and Scotland

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

The directors of a company are not legally obliged to file for insolvency if the company is insolvent, but on a practical level, filing for insolvency may be the most prudent course of action to avoid potential personal liability for wrongful trading (please see below) and to protect the interests of creditors.

There are two statutory tests for insolvency (set out in section 123 Insolvency Act 1986): cash flow test- where a company is unable to pay its debts as they fall due; and balance sheet test- where a company's assets are less than its liabilities. Both tests are relevant but the cash flow test is likely to be the more important and relevant when considering the position of directors and, in particular, at what point they may start to run the risk of incurring personal liability for wrongful trading.

Where a company is in financial difficulties, the general duties of a director continue to apply with the key difference being that the duty to promote the success of the company for the benefit of its members is made subject to a duty to:

(a) monitor the company's financial performance more frequently and assess (usually with the benefit of professional advice) whether or not there is a reasonable prospect that the company will avoid insolvent liquidation;
(b) consider, and act in the interests of the company's creditors as a whole; and
(c) take every step to minimise loss to creditors.

Generally, directors of a company with limited liability are not personally liable for the company's debts, but there are exceptions to this rule. The main insolvency exception is where the directors have not complied with duties contained in the wrongful trading provisions of the Insolvency Act 1986.

To establish a director's liability for wrongful trading, the company must be in insolvent liquidation and the liquidator must show that there was a time (*the "critical date"*), before the commencement of the liquidation, when the director knew or ought to have concluded that there was no reasonable prospect that the company would avoid insolvent liquidation. The court cannot declare a director liable, however, unless it is satisfied that after the critical date the director concerned failed to take every step, with a view to minimising the potential loss to the company's creditors, as he ought to have taken.

Directors must therefore ensure that they have up to date financial information at all times and continually assess whether there is a reasonable prospect that the company will avoid insolvent liquidation. This information should be recorded carefully in board minutes.

As soon as a director is aware that there is no reasonable prospect of avoiding insolvent liquidation he and the other directors must take appropriate action to minimise the potential loss to the company's creditors in order to avoid personal exposure.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	Yes. There are no laws or regulations that control existing lending or prohibit new lending specifically where the borrower faces financial difficulties or is insolvent. Extension of facilities will depend upon the existing contractual/security arrangements, whether new security might be subject to avoidance provisions (see section 3 below) and the creditors' willingness to extend.

3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?

If a company goes into liquidation or administration, the liquidator or administrator can apply to the court for an order to avoid or unwind certain transactions that took place in the period leading up to the liquidation or administration. In addition, in a Scottish winding up, any person who was a creditor prior to the commencement of the winding up (*a "pre-liquidation creditor"*) is entitled to challenge such transactions.

Such avoidance provisions are of direct concern to the intended beneficiaries of new guarantees or security because they may not receive what they bargain for (although it may be that the intended beneficiaries are in such a position that they have nothing to lose from taking what they can from the borrower group, for example, where they are existing unsecured lenders, on the basis that a new guarantee/security might put them in a better position in the event of a formal insolvency process). As for the directors of the companies being asked to grant new guarantees and/or security, they need advice in relation to the above-mentioned provisions because to fall foul of the provisions may be indicative of a breach of duty on their part that could lead to further repercussions such as disqualification proceedings (although that is very unlikely to be a real concern except in the most extreme and exceptional cases).

The avoidance provision which is generally of most concern to creditors considering taking security from a company in financial difficulty is the avoidance of floating charges provision. This provision applies in England, Wales and Scotland. Floating charges created by an insolvent company during the 12 months before it enters liquidation or administration are invalid, except to the extent of the value of new consideration given to the company by the lender at the same time as or after the charge was created. Where the charge is created in favour of a person connected to the company (which may be, for example, through a director or relevant shareholding) the time period is extended to two years and the company need not have been insolvent when the transaction took place. As a consequence of this anti-avoidance provision, floating charges cannot be relied upon by the creditor until the relevant one or two-year period has expired, except in relation to new advances. In addition, in Scotland a floating charge can be challenged as a gratuitous alienation (see below).

English and Welsh avoidance provisions

Companies and secured lenders must also take care to ensure that any new security or guarantee is not vulnerable to be set aside as a transaction at an undervalue (which is relatively self-explanatory), and that in giving the security or guarantee the company is not preferring the secured lender in the sense of intentionally putting the secured lender in a better position than they would otherwise have been, in the event of an insolvent liquidation. Time limits apply to both transactions at an undervalue and preferences: for transactions at an undervalue the look back period is the 24 months preceding the liquidation or administration; and for preferences, the period is 6 months unless the company and relevant creditor are connected in which case the period is 24 months.

Generally speaking, provided that a guarantee and/or security are given in return for some kind of consideration from the lender (which need not take the form of cash and could simply be forbearance), it should be safe from being successfully attacked by a subsequently appointed administrator or liquidator.

Scottish Law avoidance provisions

Gratuitous alienation- The administrator (if the company is in administration) and the liquidator and/or a pre-liquidation creditor (if the company is being wound up) (*a "challenger"*) can challenge the disposal of any part of the company's assets, claims or rights (*the "alienation"*) that took place in the 2 year period prior to the commencement of the administration/winding up proceedings (or the 5 year period if the alienation is to an associated person) where such disposal:

(i) does not fall within a limited class of exceptions;

(ii) was (in the Court's judgment) not made for adequate consideration at a time when the company's liabilities were greater than its assets (and the company's assets have not, since disposal, been greater than its liabilities); and

(iii) was, having regard to all the circumstances and in the judgment of the Court, not reasonable for the company to make.

If the alienation implements an earlier obligation, the Court would need to be satisfied that the earlier obligation was made for adequate consideration. When the proposed transaction involves providing guarantees and/or security for the obligations of an insolvent party, specific advice should be taken.

Unfair preference – a transaction that has the effect of creating a preference in favour of a creditor which prejudices the general body of creditors can be challenged by a challenger (see above). A preference created within the 6 month period of the commencement of the insolvency procedure can be challenged if it does not fall within the various exceptions. Unlike in England and Wales, there is no need to establish that there was a desire to prefer the benefitting creditor.

The day that a gratuitous alienation or preference takes effect for these purposes is the day on which it becomes completely effectual. Scottish common law insolvency avoidance provisions might also apply, but a challenge on the basis of the statutory provisions is more likely.

Lenders may be concerned to see that the shares issued to them are as close in character to the debt as possible. This is often done by issuing redeemable preference shares, which are sometimes referred to as "quasi-debt". By substituting debt for share capital, the lender will be subordinating the substituted debt to the company's other creditors and giving up any security that may be attached to the converted part. To compensate for this the lender will seek to ensure that it receives an element of "reward" from the shares i.e. a right to share in any future increase in equity value (which will be realised on, for example, a sale or listing of the company). The lender may also be able to approximate the interest that would have been recoverable under the loan through dividends. However, unlike interest on a loan, a dividend is only payable if the company has distributable profits.

The lender will want to ensure that it receives tax relief on any release of a debt to reflect its loss.

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?

The lender may (either if the loan documents provide for it or by separate arrangements) appoint a director or an observer to the board of directors, both of which would enable the relevant lender to monitor closely the decision-making process of the debtor and keep the lender informed. Director appointments can create difficult confidentiality and conflict of interest issues, and may cause the lender and debtor to be connected, which can expose the lender to certain risks (including, for example, potential liability for defined benefit pension scheme deficits and extended periods of transaction avoidance provisions, explained at 3 above). For these reasons, an observer appointment may be preferred. An observer will attend board meetings and may participate in board discussions, but does not have the ability to vote.

It is also common for lenders to distressed borrowers to require, as part of a workout transaction, a temporary increase in the level of information (financial and otherwise) that the borrowing group is obliged to provide. The lenders may also require the group to make regular presentations on their progress with the turnaround plan.

5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?

Yes, this is known as a debt for equity swap. A debt for equity swap is a capital reorganisation of a company in which a lender (or multiple lenders as the case may be) converts some or all of the indebtedness owed to it by the company into one or more classes of shares in that company.

Debt for equity swaps have become a well-trodden path in the UK as a means of addressing the over-indebtedness of a business whilst at the same time offering, to the lenders, the prospect of recovering the proportion of debt written off (and possibly, in the long term, some upside). So much so that certain investors (e.g. hedge funds) have as their strategy the purchase of distressed debt as a stepping stone towards acquiring equity in the group: a so called "loan to own" strategy.

There is no set structure for a debt for equity swap. Much depends on the existing debt and capital profile of the borrowing group and the intended result. Where the transaction involves a simple debt for equity substitution, the lender may just swap some or all of its loan for an existing class of shares in the company and with the associated restatement of the credit documents. A more sophisticated structure, for example where not all stakeholders can agree terms, might see the holding company of the troubled group going into administration or receivership, with a new company owned and funded by the lenders being established to acquire that company's subsidiaries. Or, for larger, more complex situations, a scheme of arrangement (see question 6 below) might be used to impose a debt for equity swap against the wishes of a minority of the creditors and/or shareholders.

Commercial Issues

The main commercial issues to be settled between the company (effectively representing its shareholders) and the lender are:

- How much debt is to be exchanged for share capital?
- What proportion of the total equity should the shares issued to the lender comprise?
- What class of shares should be issued to the lender and carrying what rights?
- Should the lender be subject to any restriction on its ability to dispose of the shares issued to it?

The lender's concerns

In most cases, and certainly in the case of original lenders, a lender's initial concern will be to minimise the amount of the debt to be converted (written off). This will be a matter for negotiation between the relevant stakeholders, to be conducted with the benefit of financial information and advice provided by investigating accountants.

Any institution that is to accept shares in place of debt will be keen to ensure that the number of voting shares it receives and other rights under those shares (including under any shareholders' agreement) do not lead to the institution having to consolidate the relevant company onto its balance sheet, nor trigger the need for equity accounting. Specific advice will be needed in all cases and each institution will need to consult with its auditors.

Another matter that must be reviewed in structuring the transaction is competition/antitrust law, notably the EC Merger Regulation.

Certain institutions or funds may prefer to take a warrant to subscribe for shares rather than actual shares.

Consents

Shareholder consent is usually required to issue the new shares. If the company is listed on an investment exchange, consent may be required from the relevant listing authority. The Listing Rules require that a listed company in the UK must have at least 25% of its issued share capital in 'public hands'. Additionally, if the swap results in shares representing more than 10% or more of the company's share capital being issued, a prospectus may be required. In addition, if the lender(s) ends up holding more than 30% of the shares in a public company, the Takeover Code may apply and the lender(s) may require a "whitewash" to avoid the requirement to make a mandatory offer for the company. A whitewash in this context requires the consent of those shareholders independent of the transaction. Additionally, the transaction will normally involve a shareholder/lender agreement setting out various investor consent matters and a change to the Company's constitution.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	Two restructuring tools can be used by majority creditors to cram down a dissenting minority. A company voluntary arrangement (or CVA) is an agreement between a company and its creditors, by which a company can seek to compromise its debts or agree an arrangement for their discharge. If the necessary majority of creditors approve the CVA at a creditors' meeting, then the CVA will bind all creditors (except those with preferential claims or security over the company's assets). The necessary majority of creditors is more than 50% in number of the creditors having more than 75% in value of the unsecured claims of creditors of the company (voting in person or by proxy) at the CVA meeting. Shareholders are consulted on a CVA proposal but, should they reject it, but the creditors approve it, the creditors' approval prevails notwithstanding the shareholders opposition. CVAs have not, since their creation in 1986, been used in great numbers to achieve a restructuring. That said, there has been a recent uptake in the use of CVAs, notably by retailers struggling with leases on unwanted premises. For more complex cases, including those that require an equity restructuring, a scheme of arrangement may be appropriate. A scheme of arrangement is a statutory procedure pursuant to Part 26 of the Companies Act 2006 whereby a company may make a compromise or arrangement with its members or creditors (or any class of them). The scheme is binding on all scheme creditors/members if the appropriate majority of each class of creditors/members agree. A scheme requires approval by a majority in number representing three-quarters in value of each class of creditors/members who vote at the meeting(s) convened to consider the scheme. Unlike a CVA, a scheme of arrangement must be sanctioned by the court. A big advantage that a scheme has over a CVA is that it can be used to affect the rights of secured and preferential creditors.
7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	Administration is a statutory procedure whereby a company may reorganise itself or realise its assets under the protection of a statutory moratorium. Administration is intended to work as a rescue procedure and provides scope for the company (acting by its administrator) to continue trading as usual, so far as possible, whilst discussions are held with creditors to see if a rescue plan can be agreed. In practice, it is extremely rare for a company to survive an administration. The company itself, as a legal entity, tends to end up being dissolved after its business and assets have been sold. An administration may be combined with a CVA or scheme of arrangement (see previous answer). During the administration process, the directors' powers cease and the company's business is managed by the administrator. The administrator has wide powers and may do anything necessary or expedient for the management of the affairs, business and property of the company. The administrator must endeavour to achieve one of three statutory purposes (as set out in paragraph 3 of Schedule B1 to the Insolvency Act 1986). These are to: (a) rescue the company as a going concern (the primary objective); or (b) achieve a better result for the company's creditors as a whole than would be likely if the company were wound up (the second objective); or (c) realise property in order to make a distribution to one or more secured or preferential creditors (the third objective).

1. How does a lender sell a loan?

Broadly speaking, a lender can use one of three mechanisms to sell non-performing loans:

(i) novation;
(ii) assignment (assignation in Scotland) or
(iii) sub-participation.

Novation and assignment are described below. Sub-participation is dealt with in the answer to Question 3 below.

Novation is the most frequently used method of transferring loans. On novation, there is a discharge of both the rights and obligations between the existing lender and debtor and a replacement of these by new, but usually identical, rights and obligations between the new lender and the debtor. A novation is often effected using a prescribed form of transfer certificate (as provided for in the relevant facility agreement) or, failing this, the Loan Market Association (*LMA*) form of transfer agreement with appropriate jurisdiction amendments. These documents must be signed by both the transferor and the transferee. Novation requires the debtor's consent, although this is often provided within the facility agreement when it is entered into, subject (usually) to the satisfaction of certain conditions.
Assignment is less frequently used than novation but is useful where novation is not possible (for example, where the existing lender's rights to security cannot be novated, or if the debtor is insolvent). An assignment can only operate to assign rights, not obligations. In practice, this means that if the assignor owes obligations to the debtor under the facility agreement, these obligations will remain with the assignor following the assignment. Also, upon assignment, the loan will not usually be removed from the assignor's balance sheet for the purpose of capital adequacy risk weighting. Assignment does not usually require the debtor's consent, but it is usual practice for the parties to notify a debtor of the assignment in order to perfect the assignee's interest.

2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.

In most multilateral financing structures there will be a security trustee (sometimes described as security agent), which will hold the security on trust for all of the lenders from time to time. Accordingly, an incoming lender would automatically have the benefit of the security once it becomes a lender (and the trade documentation will usually also state that the benefit of this security is sold as part of the trade).

Where there is no security trustee and the security is held by the original lender (for instance in a bilateral loan relationship) then care needs to be taken to ensure that the security is assignable and that the requisite assignment formalities are followed. In Scottish bi-lateral transactions, mirroring, additional Scottish law security might need to be granted direct to the incoming lender and additional formalities/steps are often required in relation to Scottish security.

If security over English real estate is involved then the transfer sometimes needs to be registered with the Land Registry. If fixed security over Scottish real estate (*a "standard security"*) is involved then an assignation of that interest needs to be registered with the Registers of Scotland.

Where foreign security is involved, it may be necessary to transfer the security under local law - for instance, where the relevant jurisdiction does not recognise the concept of a trust. The facility agreement may provide the relevant transfer mechanism.

3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Sub-participation is permitted. Sub-participation is the transfer of economic risk and benefit associated with the debt from a lender (Party A) to a new lender, the participant (Party B). Under the terms of the sub-participation agreement, Party A remains the legal holder of the claim and accordingly the 'lender of record', so far as the debtor is concerned. This means that Party A remains liable to the debtor for its obligations, including undrawn commitments, under the facility agreement. In turn, Party B agrees to reimburse Party A in respect of any amounts that Party A is required to advance to the debtor under the facility agreement. Additionally, Party A will agree to pass all receipts that are referable to the participated tranche to Party B, as and when they are received from the debtor. Party A will also, depending on whether or not this is included in the sub-participation agreement, act on the instructions of Party B in relation to issues such as voting. Unless there is a prohibition in the original loan agreement (which in practice is unlikely, although it is included occasionally), sub-participation can be effected without the consent of, or disclosure to, the debtor.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	No licence is required solely for the purchase or transfer of regular loans, and this does not amount to the provision of banking or investment services within the UK for the purposes of UK legislation implementing the Banking Consolidation Directive and the Markets in Financial Instruments Directive. Other regulatory approvals or licences may be required separately, depending on the nature of the entity's business. Such approvals would normally only be required for activities (including, but not limited to, accepting deposits or dealing in investments) which were not connected with the buying or selling of the loans.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	There is no statutory restriction on such purchases. Whether or not this can be done depends on the provisions of the underlying facility agreement. The taxation treatment of any such transaction also needs to be considered carefully.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	This depends to an extent on whether or not the claim is itself assignable. If the claim is assignable, and notice of the assignment is served on the insolvent debtor in the correct manner, the acquirer will ordinarily be permitted to vote on the claim in the insolvency process. This is also subject to any requirements or restrictions on assignment that are to be found in any Scheme of Arrangement or Company Voluntary Arrangement, which could in theory also restrict the ability of a creditor to assign its claims.

7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	A lender is bound by confidentiality obligations in respect of its relationship with the debtor. The facility agreement will usually contain confidentiality provisions, which will set out the circumstances in which the lender is entitled to disclose information received from, or in respect of, the debtor to a third party. For a standard LMA facility agreement this will normally include the right to pass this information to a potential purchaser of the loan, provided that the purchaser is either (a) an existing lender or (b) a bona fide potential purchaser of the loan (and that in the case of (b) the potential purchaser has entered into the LMA standard form confidentiality agreement or, sometimes, the form of confidentiality agreement provided for within the agreement). If there are no provisions in the facility agreement which entitle information to be passed to a potential purchaser then the consent of the debtor may be required in order to do so, so care must be taken in order to avoid breaching the lender's duty of confidentiality. Parties also need to ensure that information received in relation to companies/groups whose securities are traded on certain public markets is handled appropriately. For instance, information received in relation to, or by virtue of, a company's banking arrangements may be "private" and/or potentially price-sensitive, which may prevent the party holding that information from trading in the listed securities of that company and/or its affiliated parties. Breach of "insider trading" laws is a criminal offence.

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FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

When a company gets into financial difficulties, the most important question for the directors is whether or not there is a reasonable prospect of the debtor's business being able to continue. In considering this question, directors should primarily consider the company's interest rather than the shareholders' or creditors' interests. They must not prefer one creditor or class of creditors over another and they have a general duty of care to identify potential issues raised by the financial difficulties of the company; and find adequate restructuring solutions.

The key indication for a company in financial difficulties is whether it is in cessation des paiements, i.e. the company is in a situation where it cannot pay its outstanding due debts because of insufficient available cash.

Consensual procedures
A financially troubled company can opt to seek a voluntary arrangement with its main creditors without using a formal insolvency procedure. This may be achieved through negotiations with creditors in order to implement a restructuring plan. The French Commercial Code provides that such negotiations can be led by the debtor (if he so chooses) under one of the following procedures: the mandat ad hoc or the conciliation.

In the mandat ad hoc procedure, a court-appointed agent assists the directors to negotiate with one or more creditors to achieve a consensual and confidential settlement. This procedure is available only if the debtor company is not already in cessation des paiements.

Alternatively, a company in financial difficulties (or one that has been in cessation des paiements less than 45 days) can use the conciliation procedure. The aim of this procedure is for the company, under the supervision of a court-appointed agent, to negotiate a workout agreement with its main creditors.

The success of these consensual procedures (which usually include a rescheduling, and/or a partial waiver of debt) depends in practice on the consent of all the company's main stakeholders.

Insolvency procedures
Under French law, there are three insolvency procedures: the sauvegarde (which is a procedure to rescue the business of the debtor company); the redressement judiciaire (which is a procedure also aimed at rescuing the business of the insolvent company either by reorganising the company, or by a global sale of its business and assets to a third party); and the liquidation judiciaire (which is a procedure involving either the going-concern sale of all or part of the business and the assets of the debtor, or the cessation of the business and the sale of its assets for the satisfaction of its creditors).

A sauvegarde procedure can be opened by the court when the debtor is facing difficulties that it is unable to overcome by its own means but is not yet in cessation des paiements. The main difference with a consensual procedure is that it allows the debtor company (whose debts are frozen as from the judgment opening the sauvegarde proceedings) to be restructured under the court's supervision, and where the appropriate creditor majorities are obtained, dissenting minority creditors can be crammed down.

The other two insolvency procedures (i.e. *redressement judiciaire or liquidation judiciaire*) must be opened by the Court when the debtor applying for it is in cessation des paiements. An insolvent debtor is required to file a request for the commencement of insolvency proceedings (either a *redressement judiciaire* or a *liquidation judiciaire*) with the relevant Court within 45 days of the date of cessation des paiements.

In liquidation proceedings (*liquidation judiciaire*), the de jure and any de facto managers can be held personally liable (collectively or individually) for all or part of the insolvent company's debts if there is a deficiency of assets against liabilities, and the commercial court is satisfied on the evidence that there has been mismanagement and that the deficiency of assets is to some extent attributable to mismanagement or breach of duty (*faute de gestion*).

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?

If it can be established that the financial support of a creditor (not just a bank creditor) abusively delayed the date of cessation des paiements or created a false impression of solvency towards third parties, French courts consistently rule that the creditor concerned may be held liable for the increase of the debts of the insolvent company starting from the date when this abusive financial support (soutien abusif) began. The legal grounds for such liability of creditors are found in the general rules of non-contractual liability (Article 1382 of the French Civil Code).

However, a new Article L. 650-1 has been introduced in the Commercial Code (by the Law n° 2005-845 dated 26 July 2005) to protect creditors (mainly credit institutions) from liability for abusive financial support when an insolvency procedure has been opened. This is subject to certain exceptions (fraud, clear interference with the debtor's business or taking excessive security interests) under which the previous regime remains in force. The precise scope of this new protective provision is still the subject of debate and requires judicial clarification.

3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	French law contains the concept of a suspect period (période suspecte) which, broadly, begins on the date a court considers that the company became unable to pay its debts (cessation des paiements) and ends on the date insolvency proceedings are opened. Certain acts or transactions made or entered into during the suspect period are either automatically void, or can be declared so by the court. For example, new security granted during the suspect period to secure a pre-existing debt could be declared void by the commercial court, on the request of the administrateur judiciaire or liquidateur judiciaire of the company. If, in order to delay the opening of insolvency proceedings, the debtor obtained funds by overly expensive means, the debtor's manager(s), and possibly in certain circumstances the lender, could be held liable. If a company attempts to restructure using a conciliation procedure but subsequently ends up in insolvency proceedings, creditors who provided new money, goods or services in order to ensure the continuation of the distressed company's business during the conciliation procedure rank in priority of payment over: (i) all pre-insolvency proceedings claims except the wages of the employees; and (ii) most of the post-insolvency proceedings claims except (a) employee wages and redundancy payments and (b) certain expenses of the insolvency proceedings, namely the fees of the court appointed officers and the fees and legal costs deriving directly from litigation proceedings which developed during the observation period, provided, in both cases, that the court approved the conciliation final agreement. This priority does not apply to shareholders providing new equity, or creditors in respect of credit advanced prior to the beginning of the conciliation procedure.
4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	It is not advisable for the company's main lender be involved in the management of the company in order to monitor the company more closely than the usual information covenants in the credit agreement permit. If the lender is found to have interfered with, or unduly influenced, the management of the company, the lender may be held to be a de facto manager, and as such will be potentially liable to the same extent as the de jure managers for the company's debts (see the answer to question 1 above).
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Provided the company is not in cessation des paiements, or formal insolvency proceedings, a creditor may exchange debt for equity by contributing its debt claim in return for newly issued shares as part of a share capital increase. The usual rules in relation to capital increases must be complied with and necessary shareholder consents obtained. If the company is already in insolvency proceedings, a debt for equity swap is possible in either sauvegarde proceedings or redressement judiciaire proceedings . In these proceedings of sauvegarde or redressement judiciaire, according to new Article L.626-30-2 of the Commercial Code, the creditors' committee may propose debt for equity as part of the debtor's restructuring plan, which can be voted through by the requisite majority of creditors by the creditors' committee (see the answer to question 6 below). The proposal would, however, also require the approval of the court and a general meeting of shareholders. This type of debt for equity exchange is not very common.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?

In French law, the general principle is that nobody can compel dissenting creditors to agree with the terms of a debt restructuring plan. An exception to this principle is provided for by Article 1244-1 of the Civil Code, which enables a judge, at the debtor's request and taking into account the debtor's position and the creditors needs, to postpone or reschedule the payment of sums due (over a period of up to 24 months).

Also, as an exception to the general rule insolvency proceedings can be used to force a dissenting creditor to sacrifice more of its rights without its consent. In sauvegarde or redressement judiciaire insolvency proceedings, a restructuring plan can be forced on a dissenting minority of creditors in two circumstances.

The first method is by creditor committee decision. If the debtor's size exceeds prescribed thresholds, two creditor committees are formed to consider the restructuring plan. One committee comprises all the debtor's banks and financial institutions and the other comprises the debtor's main trade creditors. The restructuring plan can be approved if it is voted for by members accounting for at least two-thirds of the claims of the voting creditors of each committee. The debtor's proposals are also presented to bondholders (if there are any) at a general meeting of bondholders held for that purpose (similar to a creditors' committee). Once approved by the creditors' committees and, if it exists, the bondholders' meeting, the court must also approve the restructuring plan.

The second method by which a dissenting minority of creditors can be bound by a restructuring plan is that the court can impose a rescheduling of payments (over a period of up to 10 years) on creditors in sauvegarde or redressement judiciaire proceedings. This is so even if the plan has not been approved by one or more creditors' committee. However, the court cannot, without a creditors' committee decision, force dissenting creditors to waive any debt.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?

Apart from the preventive procedures (mandat ad hoc and conciliation), the purpose of which is to solve the financial difficulties of the debtor by a consensual arrangement entered into with its creditors, both the sauvegarde and redressement judiciaire procedures enable the debtor to continue to trade and to look for a solution that will enable the company to survive. Within these two procedures, a deal may be made with some creditors through the creditors' committees (see the answer to question 6 above). However, the final solution is ultimately decided by the court, which can impose a rescheduling of debts on unwilling creditors.

If a sale of the company's business or assets is appropriate, this can be achieved both in redressement judiciaire proceedings when a plan de redressement is not possible, and in liquidation judiciaire proceedings provided, in the case of liquidation judiciaire, that the commercial court has authorised the continuation of the business activity of the debtor to enable third party offers for the purchase of all or part of the business of the debtor to be considered.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?	To the extent that the underlying credit agreement allows assignment of part or all of the underlying rights and obligations, non-performing loans may be transferred on the basis of a written assignment agreement. In such case, the assignment would be effective against the borrower when notified of the assignment by either the assignor or the assignee. Any assignment of a non-performing loan must be part of either: (i) a syndication (i.e. to a credit institution); (ii) a securitisation (i.e. to a securitisation vehicle); or (iii) a sale of the underlying receivables (provided that the underlying receivables have matured (please see the answer to question 4 below)).
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	If the original loan agreement allows assignment of the non-performing loan, and the loan is transferred to an eligible assignee, the assignee will step into the shoes of the original lender: it will acquire all security attached to the non-performing loan. Please note that in this context a novation should be avoided, because if the loan were novated, the assignee would lose the priority attached to the security.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	A lender may enter into a sub-participation agreement pursuant to which the sub-participant does not become a party to the credit agreement, but merely takes on the underlying risks. In this case, no true sale occurs and the original lender remains liable for obligations contained in the underlying credit agreement. The sub-participant must be a credit institution.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	Sale and/or transfer of non-performing loans does not generally require a licence. Under French banking monopoly rules, persons other than a credit institution are not allowed to carry out banking transactions (including credit transactions) on a regular basis. However, if the underlying loan agreement is a non-performing loan, the non-performance generally triggers maturity of the loan. Purchase of matured receivables (including on a regular basis) is deemed not to constitute a banking activity, and so does not require a licence. Moreover, the French banking monopoly rules apply to the carrying out of banking transactions on a regular or habitual basis. Although this notion is appraised on a case-by-case analysis, the mere acquisition of one non-performing loan (including if the loan has not matured) does not amount to a regular or habitual banking activity.

5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	Provided it is not prohibited by the agreement between the borrower and lender or any other lenders, a borrower can buy part or all its own debt and as a result the debt is extinguished. If an affiliate buys the borrower's debt, the purchase must: (i) comply with the corporate purpose (intérêt social) of that affiliate, and (ii) not be seen to be made on behalf of the borrower. A solvent borrower can also buy into a syndicate of its own debt. However, irrespective of whether this purchase is made directly by the borrower or with the assistance or through one of its affiliates, it raises significant issues that may render the purchase impractical and/or put both the 'selling' lender and the borrower at risk vis-à-vis other creditors.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	Under French law the right or obligation to be a member of a creditors' committee is transferred to the purchaser of a debt. However, if a debt is purchased, the purchaser will only be allowed to vote in a creditors' committee after the transfer of the debt has been notified to the administrateur judiciaire.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	The law on data protection in France only applies for the benefit of private individuals. If the borrower of the non-performing loan is a private individual, any assignment must ensure that the borrower's data is protected in accordance with French data protection law. French bank secrecy laws must also be complied with (i.e. the assignee must be in a position to ensure bank secrecy). Loan agreements typically contain provisions releasing the lender from its obligation under French bank secrecy laws not to disclose the borrower's personal data, provided such disclosure is made for the benefit of (i) other banks in the context of syndication of the loan or sub-participation agreements, or (ii) credit rating agencies or their agents in the context of a securitisation.

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FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

A director is obliged to manage a company's business with the diligence of a prudent businessman, which includes a duty to ensure that he has at all times a fair overview of the company's financial situation. If directors are in breach of their duty, they may become liable to the company and/or to its creditors. If insolvency proceedings occur, the insolvency administrator must investigate any potential liability of the insolvent company's directors.

In particular, directors can incur liability for:

— not maintaining the company's registered share capital;
— granting loans to other directors, Prokuristen or other general representatives from the assets of the company that are needed to maintain the registered share capital;
— the relevant measure endangers the existence of the company (*existenzvernichtender Eingriff*) following shareholder's instructions;
— not filing for insolvency proceedings within the prescribed time limit (for more details please see below);
— not convening a general shareholders' meeting if in the annual financial statements or in interim accounts drawn up in the course of the business year, the value of the company's assets falls below 50% of its share capital; or
— making payments at a time when they were obliged to file for insolvency, this can include accepting payments from a third party debtor into an overdrawn account, thereby reducing the debt owed by the company to its bank.

Directors can also incur liability to creditors if, before insolvency proceedings are initiated, they cause the company to enter into transactions in breach of certain creditor-protection provisions that are aimed at preventing the preferential treatment of creditors in the event of the company's insolvency, or impairment of creditors' interests.

Each director of a company is under a duty to file for insolvency without undue delay, at the latest within three weeks of the company becoming either illiquid (*zahlungsunfähig* – which means that the company is unable to pay its debts as they fall due) or over-indebted (*überschuldet* – which means that the company's liabilities exceed its assets). However, the directors do not have to file for insolvency the event case of over-indebtedness if they reasonably consider that the company has a positive forecast for the ongoing business (*positive Fortführungsprognose*). As a rule of thumb, the ongoing business forecast can be considered positive if the debtor, according to its liquidity planning, is able to pay its debts when they fall due within 12 to 24 months.

If a director fails to file for insolvency within the prescribed time period, he can incur both criminal liability and personal liability for creditors' claims that arise after the date of insolvency. Directors can escape such liability only if they have acted without negligence (*Verschulden*). Seeking appropriate legal advice regarding their duties will help directors prove that they have not been negligent.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	In principle credit facilities may be extended and new credit granted to a company in financial difficulties. However, in certain circumstances a lender might be held liable by other creditors for immoral behaviour or for incitement to delay filing for insolvency. For example, a bank may incur liability if it grants or extends credit to a distressed company that is insufficient to restructure the company and merely delays the onset of insolvency for the benefit of the bank, thereby deceiving other creditors as to the solvency of the company, who consequently suffer loss. In such a case the loan agreement and connected collateral agreements may be contested by the insolvency administrator and the creditor may even be exposed to criminal liability. However, the risk of creditor liability can be mitigated if a contemporaneous external audit of the company's finances concludes that the proposed restructuring measures, including the credit facility, will enable the company to survive.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	New security that is granted for an existing loan in order to prevent the lender from cancelling the loan can be contested by a subsequently appointed insolvency administrator if it is detrimental to other creditors. The risk of challenge is particularly high if the new security is granted within the last three months before the company files for insolvency, but it can theoretically extend to any new collateral to secure old debts in the period of 10 years before initiation of insolvency proceedings. Security granted for new loans cannot generally be challenged. If the company becomes insolvent, any credit or other support (such as collateral for a third party loan) granted by a shareholder of the company is automatically subordinated and ranks after other unsecured creditors. Any shareholder loans or other similar measures, that were repaid or released during the period of one year before the filing for insolvency, can be contested and clawed back by the insolvency administrator.
4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	There is no general statutory right for a lender to supervise and/or monitor the financial situation of the debtor company. German Courts have in exceptional circumstances (for example if the lender shows good cause to believe that the borrower is attempting to remove assets from the reach of creditors, or is preferring another creditor) given the lender permission to inspect the company's books and records. However, German bank loan agreements often include information rights for the benefit of the bank. If the debtor does not provide sufficient information to the bank this may be an event of default that entitles the bank to terminate the loan agreement.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	It is possible under German law to agree to exchange certain (or all) of a lender's debt for equity in the company if it is not subject to insolvency proceedings. A number of different legal techniques and deal structures can be used to effect a debt-to-equity-swap, but all of them generate substantial legal issues and risks that need addressing. In particular, a bank might refrain from a debt-equity-swap in order to avoid the risks of subordinating its remaining loans as explained above in question 3. Typically a debt-to-equity-swap involves as a first step a reduction of the registered share capital of the company to reflect the real amount of equity remaining after netting out historical losses. The registered share capital is then increased (with the consent of at least 75% of the shareholders) and new equity is issued in return for a contribution in kind by releasing the company from all (or a portion of) its debt. The fair market value of the released (portion of the) debt must be at least as much as the nominal value of the newly issued shares, and to avoid any risks for the investor and to secure registration of the capital increase in the commercial register, this fair market value should be certified by an expert opinion of an external auditor.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	The only mechanism available under German law to compel a dissenting minority of creditors to agree to a restructuring exists within formal insolvency proceedings by means of an insolvency plan (*Insolvenzplan*). Under German law a company filing for insolvency has a choice of just one insolvency proceeding. However, once insolvency proceedings are opened, the insolvency administrator assesses the company's financial circumstances and may chose between liquidation or a restructuring, either using an insolvency plan (which is a rescue procedure supervised by a court-appointed insolvency administrator and is loosely based on the US Chapter 11 procedure) or by means of a so-called "self-administration" (which is a debtor-in-possession procedure conducted under the supervision of a court-appointed trustee). Often an insolvency plan and self-administration will be combined. The company and the insolvency administrator can draw up an insolvency plan to restructure the company and the creditors vote on it. Usually, it will be discussed with the main creditors before creditors vote on it. For the purposes of the vote, creditors can be divided into creditor-groups, according to the nature of their claims and each group votes separately whether to approve the insolvency plan. Within each group: — a majority of voting creditors must approve the plan; and — the sum of the claims of the approving creditors must equal more than half the sum of all claims. — The insolvency plan is approved if each group of creditors votes in favour. If a group of creditors does not approve it, the court can still approve the insolvency plan, if — the creditors of the dissenting group will not be disadvantaged by the insolvency plan when compared to a liquidation; — the insolvency plan provides some economic benefit for the creditors of the dissenting group; and — the majority of the voting groups approved the plan with the required majorities. If the court approves the plan, it is binding on all creditors, including any dissenting groups. It is possible that even a minority of creditors in value can outvote the other creditors if, for example, a large creditor is placed in one group and a majority of other groups with smaller creditors supports the plan.
7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	Insolvency proceedings under German law (as described in the answer to question 6 above) offer a variety of alternative strategies, including continuing to trade, and either proposing an insolvency plan to allow the company itself to survive, or realising the debtor's business and/or assets in a way that best serves the interest of the creditors. Alternative statutory procedures only exist for financial institutions and insurance companies.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?	In Germany, a lender wishing to transfer a non-performing loan (*"NPL"*) can use either an asset deal, or a two-stage method involving a special purpose entity and a share deal. In an asset deal, the lender transfers its claim for payment directly to the investor (*Forderungsverkauf und -abtretung*). The original lender and borrower remain parties to the credit facility. If a special purpose entity is being used, the lender's claims under the NPL, together with any employees and assets necessary for managing the claims, are first transferred to a special purpose entity, the shares of which are then transferred to the investor by the lender by way of a share deal. This transaction structure is preferable when the investor is interested in taking over the so-called 'platform' and specialized personnel for the subsequent work-out of the NPL and the related collateral. Using this method, the special purpose entity becomes the legal successor of the lender and thus a party to the credit facility. Consequently, the original lender ceases to be a party.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	Under German law, some collateral, such as sureties (*Bürgschaften*), mortgages (*Hypotheken*) or pledges (*Pfandrechte*) are automatically transferred by law if the underlying NPL is transferred. Other collateral, such as land charges (*Grundschulden*) or chattel mortgages (*Sicherungsübereignungen*), can only be assigned by way of a contractual agreement between the secured lender and the investor. Such agreement is usually included in the contract governing the sale and transfer of the secured NPL.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	If the true sale constitutes a commercial trade (*Handelsgeschäft*), any contractual restrictions with regard to the transferability of the claim are void. In addition, German law offers various options if the lender wants to off-load only some of the risks or benefits of the NPL, including sub-participation, or an equity joint venture with regard to the NPL. In a sub-participation, the investor takes over some or all the commercial risk from the lender. Usually sub-participation agreements are not communicated to the borrower. Where the lender and investor choose the equity joint venture method, they jointly found a company and the lender transfers the NPL (or NPL portfolio) to the joint venture company by way of a contribution in-kind (*Sacheinlage*).
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	Any person who offers banking or financial services on a commercial basis in Germany needs a banking licence. If the investor transferee of the NPL is only collecting receivables by means of a regular work-out of the NPL, no banking licence is required. However, if the investor intends to extend existing credit lines to borrowers of the NPL on a commercial basis, a banking licence is required. If the investor uses a third party for debt collection, the debt collector requires a licence (*Inkassolizenz*).

5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	German law does not prohibit the borrower or a company associated with the borrower from acquiring part of all the debt owed by the borrower to a lender/lenders. As a general rule (subject to few exceptions), if the borrower acquires its own debt, the loan automatically ceases to exist by law (*Konfusion*).
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	Yes. The investor has a voting right in the creditors' assembly if he is able to prove that the claim has been transferred to him. If the claim is disputed, the court will apply a broad estimate of the disputed claim (i.e. a percentage of the claim applied by the court in the relevant case) for voting purposes in the creditors' assembly. If the insolvency administrator or the court continues to dispute the claim in part or in full, the creditor can go to court requesting a binding verdict of the court whether the claim should be allowed or not.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	German rules in relation to bank secrecy and data protection can complicate (but not usually prevent) an NPL sale. Breach of bank secrecy or data protection laws can result in liability for damages, but they do not render the assignment of NPL void if the debtor is in default under the NPL and/or the lender has rightfully terminated the loan agreement.

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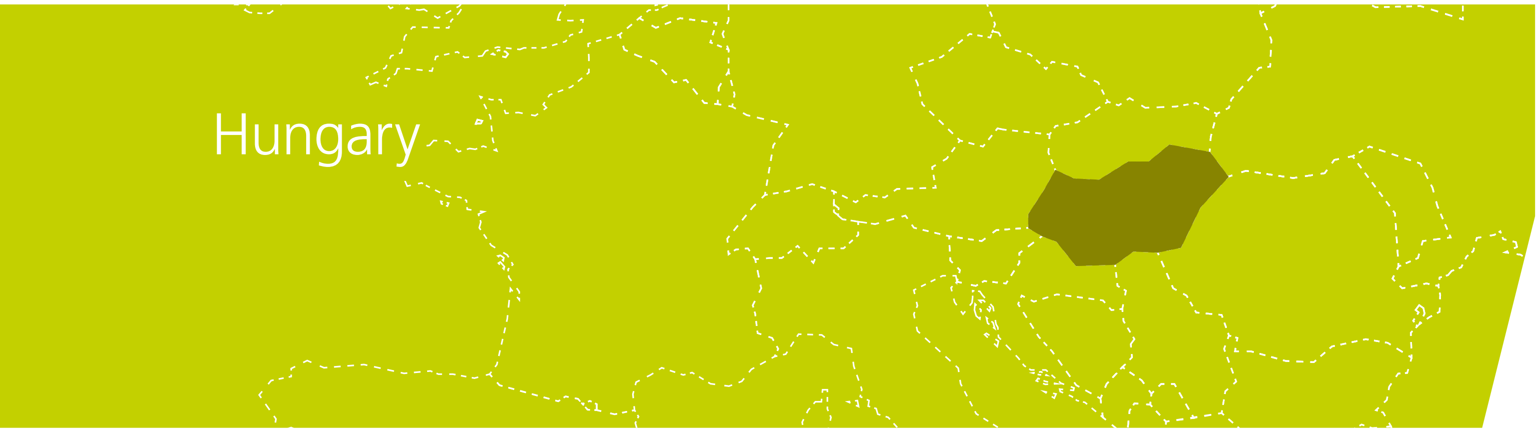

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

Hungarian law imposes a duty on executive officers to exercise due care and diligence in the management of the company. The duty applies whether the company is financially sound or distressed. If a company is facing the threat of insolvency, the executive officers must act primarily in the interests of the company's creditors, rather than its shareholders. Additionally, they must take all reasonable steps to mitigate the creditors' losses.

There is no formal obligation on executive officers in Hungary to cause the company to file for insolvency within a prescribed period. However executive officers, and any persons with power to influence the company's decision-making process, can subsequently be held personally liable if they should have reasonably foreseen that the company would not be able to satisfy its liabilities when due and should have taken action accordingly and as a result

- (i) the assets of the company decrease; or
- (ii) they frustrate the satisfaction of the creditor; or
- (iii) they fail to comply with their statutory obligations regarding contamination caused by environmental pollution. In such circumstances, the executive officers will be held liable for
  - (a) the amount by which the debtor's assets have decreased (in case of (i) above); or
  - (b) the amount of the creditor's claim that cannot be satisfied from the liquidation assets (in case of (ii) above); or
  - (c) the amount of the fine or any other liabilities incurred in connection with the environmental contamination (in case of (iii) above).

In practice therefore, executive officers tend to file for insolvency when they foresee that the company will not be able to satisfy its liabilities when due, unless the company given a rescue loan or the suppliers of the company agree to reschedule the company' s payment obligations.

One of the possible consequences of insolvency proceedings is that the executive officers can be disqualified from being executive officers of any company in Hungary for a period of five years if in a final and binding decision, the court declares the executive officer liable for the amount of the creditors' claim that cannot be satisfied from the liquidation assets and the executive officer fails to comply with this court decision. The five-year period is calculated from the time when the enforcement procedure against the executive officer made on the basis of the above court decision ends unsuccessfully.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	Under Hungarian law there is no formal restriction on extending credit facilities to a company in financial difficulties. However, certain transactions entered into by a company in a prescribed period before insolvency proceedings begin can be subsequently challenged. Vulnerable transactions of this kind include giving a preference to a particular creditor by amending an existing contract, granting security in respect of an existing debt, or entering into a transaction for no or undue consideration. In Hungarian law there is a concept of "threatening insolvency" which occurs when management or its shareholders should reasonably foresee that the company will not be able to satisfy its liabilities when they fall due. Any debts incurred after the threat of insolvency has occurred in favour of a majority shareholder are subordinated behind the company's other creditors' claims. Likewise, any security that is created in favour of the majority shareholder after the threat of insolvency has occurred will be similarly subordinated. In this context, a majority shareholder is a shareholder that controls over 50% of the voting rights in the company or has a dominant influence over it. A shareholder has a dominant influence over a company if (a) it is entitled to appoint and remove the majority of the executive officers or supervisory board members of the company; or (b) it (alone, or by virtue of an agreement with other members or shareholders of the company) controls more than 50% of the votes.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	If creditors provide "new money" at the same time any new security is created, the transaction is not regarded as preferential and the security is not vulnerable to challenge. However, certain transactions entered into prior to liquidation can be challenged. After the commencement of liquidation proceedings, the liquidator can apply to court seeking an order declaring that certain pre-liquidation transactions are invalid. Such challenges can be initiated within ninety days of acquiring knowledge of the underlying facts, but in any event, must be commenced within one year of the commencement of the liquidation proceedings. Grounds for challenge are: 1. contracts aimed at the disenfranchisement of creditors (in respect of contracts entered into within the five year period before the receipt of the request for liquidation proceedings by the court); 2. contracts for undue consideration, which are transactions at an undervalue where the consideration given by the company exceeds that which it received, or transactions for no consideration (in respect of contracts entered into within the two year period before the receipt of the request for liquidation proceedings by the court); 3. contracts granting a preference to a creditor, which is the case if a contract unduly prefers the creditor and the transaction is outside the scope of the debtor company's ordinary course of business (in respect of contracts entered into within the period of ninety days before the receipt of the request for liquidation proceedings by the court).

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	If a borrower is in financial difficulties, the lender and the borrower often contractually agree to appoint a person to monitor the activities of the borrower. Such a person is usually authorised to countersign all undertakings of the borrower, to prepare a regular report on the borrower's activities and to advise how to restructure the company and/or its debts in order to avoid insolvency. Such a person can incur shadow management personal liability in the event that he is involved in the borrower's decision-making process, which is identical to the liability of executive officers above (see the answer to Question 1 above). He may also incur corporate personal liability if he is appointed to the board of directors/managing directors or supervisory board and in both cases he votes for the approval of the resolution which results in the insolvency of the company or causes damage to a creditor and/or the company.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Yes, a debt for equity swap is a relatively common tool in practice and is a fairly straight-forward exercise. It requires the co-operation of the company, its existing shareholder(s) and/or the future shareholder(s) (if any) who wish(es) to swap the debt owed to it/them for equity, and completion of the steps set out in Act IV of 2006 on Business associations, as amended, of the Republic of Hungary (the "Hungarian Companies Act"). A debt for equity swap can be implemented during either bankruptcy or liquidation proceedings by way of a composition agreement. However, no specific laws regulate the specific steps and timeline of a debt for equity swap in this context. For the purposes of restructuring it is important to note that if the debt-for-equity swap takes place at a time when insolvency is still reasonably likely or foreseeable and the lender/shareholder retains some of its debt, it could find that its remaining claims will be subordinated to other creditors' claims and its security ignored for the purposes of the insolvency proceedings.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?

In the context of corporate rescues and restructurings, market practice tends to lean towards contractual (i.e. consensual) restructurings without recourse to formal proceedings. Bankruptcy proceedings (*csődeljárás*) in theory aim to provide the debtor company with a moratorium period during which it may agree with its creditors a court-approved plan to restructure its obligations and thereby restore its solvency. However, bankruptcy proceedings are more of a theoretical option, because in practice the process is rarely used due to legal difficulties.

Where bankruptcy proceedings are used, the company can propose a settlement agreement, which must be accepted by more than 50% of the votes of both the secured and unsecured classes of creditors and be approved by the court. If approved, the settlement agreement binds both consenting and non-consenting creditors, provided that non-consenting creditors are not discriminated against, and the bankruptcy proceedings are terminated.

Liquidation proceedings (*felszámolási eljárás*) usually focus on the enforcement of creditors' claims and the distribution of the debtor company's assets. At the end of this procedure the debtor company is dissolved. However a compromise with the creditors is also possible in liquidation proceedings if it is concluded within the period starting 40 days following the commencement of the liquidation proceedings and ending with the submission of the final financial report by the liquidator.
A compromise agreement must be approved by creditors holding at least
(i) 50% of the votes in all classes; and
(ii) at least two thirds of the total claims.

Creditors with disputed claims cannot vote but their claims can still be satisfied if the relevant court establishes that their claims are well-grounded and due. If the agreement resolves the insolvency of the debtor company and satisfies all the relevant legal criteria, the bankruptcy court can approve it and the liquidation proceedings are terminated. If approved, the compromise agreement binds all creditors (including those who did not vote for it). If the agreement is not approved, the liquidation proceedings continue.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?

Bankruptcy proceedings, described in the answer to question 6 above, can be used to enable the company to continue to trade and explore a consensual deal with creditors to ensure its survival.

Liquidation proceedings (also described in the previous answer) can also be used to explore a compromise with creditors, or a sale of the company's assets, but in liquidation proceedings, the company does not automatically continue to trade. The decision rests with the liquidator, subject to the consent of the creditors' committee. If no consensual deal is possible, the liquidator will sell the debtor's assets and distribute the proceeds to the company's creditors.

DISTRESSED DEBT TRADING	
1. How does a lender sell a loan?	Pursuant to Hungarian law, non-performing loans can be sold by way of assignment. No formalities are required for an assignment and the debtor need not be notified in order to perfect the assignment. However, notification is required to enforce the assignment because until the debtor is notified the debtor can still discharge the debt by paying the assignor.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	Pursuant to Hungarian law, certain types of security, known as ancillary security, transfer automatically with an assignment of the corresponding loan. Examples of ancillary security include a mortgage over real estate, a fixed charge, a floating charge over inventory and security deposits. Where the security is registered it is advisable to register the transferee in the relevant register. Other types of security, known as non-ancillary security do not transfer automatically and must be transferred independently, or recreated in favour of the transferee. Examples of non-ancillary security include: an independent pledge (i.e. a pledge that is created over any type of asset that is independent from the claim); a security assignment (i.e. the transfer of rights and claims for security purposes); and option rights (i.e. a put option or right of purchase for security purposes). In order for a security assignment or an option right to be transferred to the new lender, the claims (in case of a security assignment) and the subject of the option right must be transferred back to the borrower and the borrower must grant the security afresh to the transferee.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	There are no restrictions in Hungarian law on sub-participation agreements. If a true sale is prohibited by the credit agreement, either the lender may enter into a sub-participation agreement with sub-participants (i.e. financial institutions) who take over the underlying risks, or the lender may establish an SPV and transfer the non-performing loan into it together with any related security. In a sub-participation transaction, it is not strictly necessary to re-register the sub-participants as the beneficiaries of any related ancillary security but it is often advisable in order to avoid any dispute over identity of the true real beneficiary of the security and to make any enforcement of the security easier.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	A one off purchase of a non-performing loan does not require a licence, but purchasing non-performing loans as part of a business would qualify as providing a financial service for the purposes of Hungarian law, and would consequently require a licence from the Hungarian Financial Supervisory Authority.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	Hungarian law does not prevent a borrower from buying its own debt. If a borrower does acquire its own debt, then the debt ceases to exist.

6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	A person who purchases a claim against an insolvent company after the commencement of liquidation proceedings can acquire the right to vote and claim in the insolvency process if either the transferor was already registered as a creditor in the proceedings or the deadline for registration (see below) has not yet lapsed and the transferee registers the claim. Claims have to be submitted within forty days of the publication of the liquidation proceedings in the Companies Gazette and a fee is payable towards covering the liquidator's costs. The registration fee payable is 1% of each creditor's claim subject to a minimum of approximately 18 Euros and a maximum of approximately 720 Euros. If a secured creditor fails to submit its claim within the 40 day deadline, it is possible to make a late submission before the final cut off date of 180 days from the commencement date. Late filing may result in the loss of the benefit of any security or priority. Provided the transferor is already registered as a creditor in the liquidator proceedings, there is no need for the transferee of the claim against an insolvent debtor to re-register as a creditor in the liquidation proceeding because he takes over all rights of the transferor. As set out in the answer to Part II question 1 above, notification of the insolvent debtor is required in order to enforce the creditor's right.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	The Act CXII of 1996 on Credit Institutions and Financial Enterprises regarding data protection and bank secrecy applies. Pursuant to this, bank secrets can be disclosed to third parties if it is in the financial institution's interests to sell its receivables or for the purposes of collecting its outstanding receivables.

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FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

Under Italian law, the directors of a company are under a general duty to preserve the company's assets. They can be held personally liable if their negligent behaviour causes loss.

There is no statutory definition or test for insolvency in Italian law, but case law has established that a company is regarded as insolvent when it is in default, or there is other external evidence that the company is unable to pay its debts as they fall due, for example if the company's registered office is shut down or the company is asset-stripped.

If a company becomes insolvent, the company's directors should, in theory, file immediately for declaration of bankruptcy (*fallimento*). More usually, however, the directors apply for a composition with creditors (*concordato preventivo*), which is a flexible preventive procedure designed to restructure the company's debts, or to achieve a sale of the company's business or assets. The composition proposal must be approved by the majority of creditors and ratified by the court to become binding on all creditors.

Where a company is balance sheet insolvent (in the sense that its indebtedness exceeds its net assets) or requires a capital contribution, any shareholders' loans are treated as subordinated to other creditors' claims. If a shareholder's loan is repaid in the 12 months before a company is adjudged bankrupt, then any monies repaid in breach of this principle can be clawed back by the receiver, and the directors can be held liable to the company and its creditors for the damages incurred by them as a consequence. In addition, directors who are found guilty of "reckless bankruptcy" (*bancarotta semplice*) (which is concealing, dissipating, diverting or destroying the company's assets, or fabricating liabilities) may be imprisoned for a period of between six months and two years. The more serious offence of "fraudulent bankruptcy" (*bancarotta fraudolenta*), which is where directors have made an unfair profit or have caused damage to the company's creditors, carries a prison sentence of three to ten years imprisonment.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?

Italian legislation does not restrict lenders from extending facilities to a company in financial difficulties.

However, in 2006 the Italian Supreme Court ruled that a bank could be liable to another creditor of an insolvent borrower if it granted credit to the insolvent borrower and by doing so concealed the borrower's financial predicament, creating an illusion of creditworthiness towards other creditors. A bank can also be liable to the company in an action by its receiver if the behaviour of the bank triggered the company's insolvency or worsened its financial situation.

3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	The receiver in bankruptcy of a company has the power to claw back certain payments and avoid certain guarantees or security entered into in the "suspect period" preceding the declaration of insolvency. In particular, the receiver of a company subject to insolvency proceedings may avoid: (a) any security created within one year preceding the declaration of insolvency in respect of existing debts which at that time were not yet due and payable; and (b) any security created within six months preceding the declaration of insolvency in respect of existing debts which at that time were due and payable, unless the creditor can prove that it was not aware of the insolvency of the debtor. This is quite difficult to prove. Furthermore, the receiver can apply to court to challenge any security created within the six month period preceding the debtor's declaration of insolvency in respect of debts arising at the same time as the creation of the security, if he can prove that the creditor was, or should have been, aware of the debtor's insolvency at the time. A successful challenge results in a judicial declaration that the security is ineffective. There are exemptions to the above claw-back provisions where the payments, guarantees or security were entered into as part of a composition with creditors (*concordato preventivo*), or an extraordinary administration procedure (*amministrazione straordinaria*), or a restructuring plan (*accordi di ristrutturazione*) that has been ratified by the court, or one that is put in place under the certified restructuring plan procedure (*piani attestati di risanamento*). It is, therefore, advisable for lenders or existing creditors wishing to extend support to a company in financial difficulties to do so only within the framework of the rescue and restructuring procedures referred to in this paragraph or on the basis of a plan certified by an authorised auditor.
4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Under Italian law, lenders do not have the right automatically to appoint a director or observer to the borrower's board. If a lender wishes to make such an appointment, it may only do so if the loan document so provides, or it reaches agreement with the borrower, or if it holds voting rights as a result of a pledge over the company's shares or quotas as part of a security package. However, once appointed, the new director will be subject to the same duties and responsibilities as the borrower's other directors, and he cannot act exclusively in the lender's interests. As a general rule, a lender that appoints a director to a borrowing company does not expose itself to risk in relation to the appointment provided the lender does not exercise control over the nominated director.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	The Bank of Italy (*Istruzioni di Vigilanza*) rules permit a bank to convert its loans into shares of commercial companies in financial difficulties, provided that certain requirements are met (e.g. a restructuring plan is agreed by the major lenders of the company). A debt to equity conversion can also be achieved in practice by a lender with the benefit of a share pledge enforcing the pledge. If a debt to equity conversion results in a lender holding shares in a company listed on the Italian Stock Exchange (*Borsa Italiana*) above certain thresholds (2%, 5%, 10% etc), the holding must be notified to the Italian Stock Exchange Authority (*Consob*) and to the participating companies.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	A composition with creditors (*concordato preventivo*) (also referred to in the answer to question 1 above) is a court-supervised restructuring. Creditors representing at least 51% in value of the unsecured claims admitted to vote must approve the restructuring proposal. If the concordato proposal provides for the full payment of secured creditors, they are admitted to vote only to the extent that they waive their secured rights. The concordato proposal can provide for the creation of different classes of creditors and different treatment among the various classes of creditors. Once creditors have approved it, the court must ratify it and the proposal is then binding on all creditors (including those who did not vote for it, or did not vote at all). As an alternative to the concordato preventivo procedure, the company can propose a consensual restructuring plan (*accordi di ristrutturazione*), which is normally based on a restructuring agreement entered into between the company and the main creditors (especially banks). The restructuring plan needs to be approved by creditors representing at least 60% in value of all the company's debts, and it must also be endorsed by an expert, who assesses the practicability of the plan as well as the company's ability to pay all the creditors that do not participate in the plan. The proposed plan must be filed at the Companies Register, following which, other creditors and any interested third parties have 30 days to raise objections. Provided any objections are defeated, the Court will ratify the plan and it is binding on all the company's creditors whose claims are compromised by the plan.
7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	Where a company is pursuing a composition with creditors (*concordato preventivo*) (see previous answer), the company can continue to trade under the management of the administrator, monitored by the court-appointed commissioner (*commissario giudiziale*). The procedure can achieve either a restructuring or sale of some or all of the company's assets or businesses. In a restructuring plan procedure (*accordi di ristrutturazione* – see previous question), the company's directors retain their management powers to conduct the company's business without any form of control by the court. Italian law provides for two additional extraordinary administration procedures for large companies in insolvency, namely extraordinary administrative procedure (*amministrazione straordinaria delle grandi imprese in stato di insolvenza*) and compulsory winding-up (*Liquidazione Coatta Amministrativa*). The purpose of an amministrazione straordinaria is to preserve the company's assets, which contrasts with the purpose of a liquidazione coatta amministrativa, which is to liquidate them. Amministrazione straordinaria is available to a company that has at least 200 employees, and an overall indebtedness equal to at least two thirds of both the value of its balance-sheet assets and operating revenue as reported in the last financial statement. Liquidazione coatta amministrativa is a procedure for specific types of companies (for example, banks, insurance companies, and financial intermediaries). In this specialist procedure, the administrative authority has certain powers that are normally reserved to the court in ordinary insolvency procedures.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?	Credit can be transferred under Italian law by way of an assignment agreement. The borrower's consent or acceptance is not required, but in order to make the assignment enforceable against the debtor and third parties (including any possible subsequent assignee of the credit), the debtor should be notified of the assignment, by way of a communication bearing a data certa (i.e. a date certain at law, which is an official date stamp or seal that has been affixed using a stamp of the post office or a seal of a notary public or any other public officer). If the borrower is not notified of an assignment, it can obtain a discharge by payment of the outstanding loan balance to the assignor (unless the assignor is given evidence that the borrower was aware of the assignment). Furthermore, if the loan is subsequently assigned to or pledged in favour of a third party, such latter assignment will prevail if it has been notified to the debtor. If the lender wishes to assign not just the credits arising under a loan agreement but also the loan agreement itself (including the lender's obligations), the transaction would amount to an assignment of a contract, and the counterparty's consent would be required.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	The assignment of credits triggers the transfer of all the associated privileges, charges and security. Where the assigned credits are secured by a mortgage, the assignment must be noted in the relevant Land Register. If the credit is secured by a right of pledge, it is necessary to transfer the underlying asset to the assignee or to record the transfer in the relevant ledger and certificates (e.g. in the case of a pledge over shares/quotas). In case of a bulk assignment of financial credits pursuant to Article 58 of the Legislative Decree no° 385 of 1 September 1993 (the "Banking Consolidated Act"), the transfer of any security automatically takes place upon publication of the assignment in the Italian Official Gazette.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Italian law makes no express provision for sub-participation agreements. Normally subparticipation is effected by (and consequently treated as) an assignment of the contract or an assignment of the underlying credit and therefore is subject to the relevant Italian law provisions. In particular the assignment of a contract must be authorised by the counterparty (unless such authorisation has been already granted in advance as normally happens in facility agreements). The debtor's consent is not required for an assignment of debts.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	Under Italian law, the sale and purchase of credits or loans on a professional basis falls within the definition of financial activities and therefore can only be carried out by banks and financial intermediaries, duly authorised according to Article 106 and 107 and 113 of the Banking Consolidated Act. On the basis of the above, the assignment of a loan contract can only be carried out in favour of banks and financial institutions duly authorised to carry out such (regulated) activities.

5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	Such a transaction would in principle be permitted, although it would be quite unusual.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	Under the Italian insolvency procedures, creditors of insolvent companies are not actively involved in the decisions related to the management of the procedure and their vote is required only if they are members of the creditors' committee. If the party acquires its claim through assignment from another creditor whose claim is already admitted in the insolvency procedure, there is no need to apply for the claim to be re-admitted, but the third party creditor is not entitled to be substituted for the assignor on the creditors' committee.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Italian data protection laws do not prevent the sale or transfer of non-performing loans, but the data transfer must be notified to the borrower, and the assignor must abide by data storage and data processing obligations. Some exemptions apply to bulk loan transfers, for example securitisation transactions.

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The Netherlands

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company gets into financial difficulties? Specifically: are the directors legally obliged to file for insolvency if the company is insolvent? Assuming the circumstances are such that the directors are not obliged to place the company in a formal insolvency procedure, are there steps that a board of directors should be advised to take to mitigate their personal exposure/risk?

Directors are under a duty to manage the company properly. This duty is owed to all the stakeholders (including employees and creditors), not just the shareholders, but if a company gets into financial difficulties, the duty becomes owed primarily to the creditors. Breach of this duty can result in personal liability for the company's debt.

There are several ways that a director can be held personally liable for the company's debt after it has entered bankruptcy proceedings. In restructuring situations, however, a director's primary concerns will be to avoid potential liability for causing the company to enter into a transaction at a time when the company cannot fulfil its obligations; and causing the company to make a preferential payment.

Under Dutch law directors are not legally obliged to file for insolvency if a company is insolvent, but directors can be exposed to personal liability as mentioned above, if they fail to take appropriate steps in the circumstances.

Steps that a director can take to reduce the risk of personal liability include the following:

— If the company's financial situation is precarious, this should be regularly discussed in board meetings and all discussions and decisions should be adequately documented.
— Call a general meeting of shareholders and the supervisory board and inform them about the company's financial status and financial difficulties.
— Inform the tax authorities as soon as it is forecast that the company will not be able to comply with its tax obligations.
— Obtain adequate directors´ liability insurance.
— Obtain a final discharge resolution from a general meeting of shareholders for the directors' management.
— Ensure that the company has complied with all mandatory publication and registration duties (e.g. annual reports etc).
— Do not let the company incur credit if it is obvious it will not be able to repay.
— Do not overstate the creditworthiness of the company.
— Obtain professional (legal, tax and financial) advice.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?

This is not a problem under Dutch law. There is no penalty for extending non-performing loans or granting new loans to insolvent companies. However providing extra security can be an issue (please see the answer to question 3 below).

3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	Under Dutch law there is a legal concept of directors´ liability for payments towards a specific (group of) creditors (referred to as selective or preferential payments) where the interests of other creditors are neglected as a result. In addition, the pari passu and negative pledge provisions in credit facilities normally require the directors to negotiate with the company's main creditors prior to creating any additional security. During bankruptcy proceedings, the trustee can challenge the company's earlier decision to grant additional security. If the company was contractually bound to provide security – which is common practice - it is difficult to successfully challenge the transaction. The trustee in bankruptcy will have to prove that creditors were aware of a pending filing for bankruptcy, or prove that the creditor and the company conspired in order to put the creditor into a better position than the other creditors.
4. If a company's main lender wants to monitor the company very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Dutch law does not provide creditors with special information rights. However, if an event of default has occurred, the lender has more leverage to negotiate wider information covenants in any renewed credit facility. Creditors generally do not appoint representative members to the board of directors or the supervisory board. Such an appointment might require prior approval from the Netherlands Central Bank (*DNB*) if the lender has a Netherlands banking licence. The appointment of creditor observers to the board of directors is also not a common practice in the Netherlands. Under Dutch law there is a risk of shadow director liability if the creditor significantly influences policy decisions within the company.

5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?

The exchange of debt for equity in the company requires the cooperation of existing shareholders because the articles of association of a Dutch private company with limited liability (*besloten vennootschap*) contain so-called blocking provisions.

In order to become a shareholder of a company, the agreement providing for the transfer of the shares will have to be executed by a civil law notary. If the company has to issue new shares this also requires a deed executed by a civil law notary.

A lender that acquires shares in a distressed company must be also be aware of the risk of shadow director liability if the shareholder significantly influences policy decisions within the company.

If as a result of a debt for equity swap in a distressed borrower, the lender holds more than a certain percentage of the company's shares, or voting rights of shares, or of a particular class of shares, the company could become one of lenders' subsidiaries for financial reporting purposes.

Pursuant to the Financial Supervision Act (*Wet op het financieel toezicht*), lenders with a banking licence and a registered office in the Netherlands will also require a declaration from the Dutch ministry that no objections have been raised prior to the transfer of the shares, if as a result of the swap, the bank owns 10% or more of the issued shares of a company that is active in the Dutch financial industry (e.g. a Dutch bank, insurer, investment institution). If a Dutch bank passes the 10% threshold with regard to shares in other companies (foreign financial, Dutch non-financial), this does not result in an obligation to obtain such declaration except where the balance sheet of this company is larger than 1% of the bank's balance sheet.

There are some additional issues to be taken into consideration if a lender enters into a debt for equity swap in relation to a listed borrower, including (but not limited to):

- The requirement on a shareholder to make a mandatory offer for the company when it acquires (or persons acting in concert acquire) an interest in shares of the company that carry 30% or more of the voting rights.
- If the borrower swapping debt for equity is a certain type of securities-issuing institution, then it must disclose any shareholdings or voting rights that reach, exceed or fall below several different percentage thresholds ranging from 5% to 95%. In addition, there is also a duty to disclose ownership of shares with special controlling rights.
- Market abuse rules must be adhered to.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are open to the company/the majority creditors to compel the minority of dissenting creditors to agree?

Outside bankruptcy proceedings, there are no mechanisms under Dutch law that compel creditors to agree to a debt restructuring.

In bankruptcy proceedings, the ordinary creditors of the company can agree to a scheme of composition (*akkoord*) proposed by the bankrupt company. If the majority of the ordinary creditors representing at least 50% of the total outstanding ordinary debts approve the scheme, it will bind all ordinary creditors, including the dissenting minority. Creditors with priority (*voorrang*) are not bound by the scheme and are therefore not allowed to vote on it. These creditors include creditors with claims secured by a mortgage or pledge and any other creditors who have statutory priority rights over other creditors (*voorrechten*), such as tax authorities.

Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business for as much money as possible?	A company in financial difficulties can choose between two statutory procedures: (i) suspension of payment (*surséance van betaling*), aimed at the continuation of the company; or (ii) formal bankruptcy (*faillissement*), aimed at liquidation of the company. The purpose of a suspension of payment is to give the debtor an opportunity to reorganise, search for new means of financing its debts and continue its business. An administrator (*bewindvoerder*) and a supervisory judge are appointed to oversee the restructuring activities, and all measures of recourse from ordinary creditors are suspended, while creditors with priority rights are not affected. Debtors often postpone requesting a suspension of payment as typically, such a request leads to a substantial loss of confidence by third parties. As a result, the request for suspension of payment tends to be too late and in most cases the suspension is eventually converted into a formal bankruptcy. Most successful company rescues start at an earlier stage, prior to suspension of payment. When a consensual deal cannot be achieved, a formal bankruptcy procedure allows for the sale of the company's assets in an orderly manner. In both procedures the courts can order a two month insolvency stay (cooling-off period), which can be renewed for another two months if necessary. During the cooling-off period third parties cannot enforce any rights against assets that are in control of the debtor or the trustee in bankruptcy without the approval of the supervisory judge.

DISTRESSED DEBT TRADING

1. What are the basic requirements of a "true sale" of a non-performing loan (e.g. how does a lender transfer a non-performing loan)?	There are theoretically three ways to achieve a transfer of a non-performing loan: assignment, transfer of contract (*contractsoverneming*), or novation. Under an assignment, only the rights, and not the obligations, of the creditor are transferred. A transfer of the creditor obligations can be accomplished by way of a takeover of debt (*schuldoverneming*), requiring the consent of the debtor. A non-performing loan, which constitutes receivables or registered instruments (*rechten op naam*), can be transferred either by way of a disclosed assignment (*openbare cessie*) or a non-disclosed assignment (*stille cessie*). A transfer by way of disclosed assignment requires (besides the assignor's title to the receivables or registered bonds) a deed of transfer and a notice to the debtor from either the assignor or the assignee. A transfer by way of non-disclosed assignment requires (besides the assignor's title to receivables or registered bonds) either a notarial deed of transfer or a deed of transfer registered with tax authorities. The transfer of a non-performing loan, that consists of bearer instruments requires (besides the transferor's title to the instruments) a deed of transfer and the granting of possession (*bezitsverschaffing*) of such bearer instrument. In a transfer of contract, the rights as well as the obligations transfer from the lender to the buyer of the debt and requires the cooperation of the borrower. It is possible to novate a loan agreement under Dutch law, but novation should be avoided in the Netherlands, because any security associated with the loan will be lost.

2. Are the various forms of security in relation to the non-performing loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the non-performing loans.	In the case of novation the security is not automatically included in the transfer. In the case of an assignment or transfer of contract, pledges and mortgages securing the loan are automatically included in the transfer. A non-performing loan will, typically be secured by either proprietary security rights (*zakelijke zekerheidsrechten*), such as the pledge (*pandrecht*) and the mortgage (*hypotheek*), or personal security (*persoonlijke zekerheidsrechten*) such as a guarantee (*garantie*). Proprietary security rights follow the secured obligations (*droit de suite*) and will therefore remain attached to the non-performing loan after such loan has been transferred (except in case of transfer by novation). Personal security rights do not have droit de suite and will have to be transferred separately to the assignee to enable it to invoke any rights arising from the security. The transfer of such security may be done by way of a separate transfer of contract (*contractsoverneming*) but it requires the cooperation of the grantor of the security.
3. If the underlying credit agreement prohibits a "true sale" (i.e. a change in the lender of record) how else (if at all) can a lender off-load some of the risk/ benefit in the loan? E.g. does your jurisdiction permit sub-participations agreements?	Under Dutch law, a lender can off-load some of the risks of a loan by (i) syndication of loans, (ii) sub participation or (iii) credit insurance. See also the answer to question 4 below for regulatory considerations.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of non-performing loans? Would it qualify as provision of banking/financial services in the territory of the assignor or the borrower?	As long as it does not concern consumer loans, there are no specific licensing or authorisation requirements under Dutch law, because the purchase, sales and/or transfer of (non-consumer) non-performing loans will not qualify as the provision of banking or financial services. For Dutch borrowers there is a regulatory duty only to borrow money from professional market lenders if the amount borrowed is less than fifty thousand euro (EUR 50.000). This should be kept in mind when sale, syndication, sub participation or other transfer is contemplated.
5. Is a borrower or a company associated with the borrower permitted, as a matter of law (i.e. assuming that the credit agreement does not expressly prohibit it), to buy certain of the debt that it owes to a lender/ lenders?	There is no provision in the Dutch legislation that prohibits a borrower (or a company associated with the borrower) from buying its own debt. If a borrower buys back its own debt, the debt ceases to exist.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the acquirer of the claim/debt have the right still to vote that claim in the insolvency process?	Under Dutch law any creditor of the insolvent company has a voting right. Dutch insolvency law does not prohibit a new creditor from voting. Therefore, to the extent a claim against the insolvent company has been acquired by a new creditor, it will also acquire the assigning creditors voting right.

7. Are there any issues regarding data protection and bank secrecy laws in your jurisdiction which would hinder or prevent a lender from selling and/or transferring non-performing loans?

This is only an issue if the documentation pertaining to the non-performing loan that is being transferred contains personal data (i.e. data that - directly or indirectly - identifies a natural person). If this is the case, the sale or transfer of the loan will have data privacy law implications. The transfer of the personal data (as well as further use thereof by the buyer) is subject to the Dutch Data Protection Act (*Wet bescherming persoonsgegevens (the "DDPA")*). The transfer of personal data is only allowed if one of the statutory justification purpose applies, and the transferor informs the data subjects of the transfer.

The transfer may be considered to be in the legitimate interests of a natural or legal person, as referred to in Article 8f of the DDPA/Paragraph 7 Directive 95/46/EC. If the assignor is based in Europe, but the transferee is not, the transfer of personal data requires a permit from the Ministry of Justice, unless the data subject has given its unambiguous written consent for the transfer of its data to recipients outside the European Economic Area.

The data protection rules are not an issue in the case of a disclosed assignment, but in the case of an undisclosed assignment it may lead to complications.

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Poland

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

Regardless of whether a company is in financial distress or not, the directors are obliged to put the interests of the company first. Under Polish law creditors have the right to challenge any actions taken by a company that may potentially affect the company's ability to repay its debts. For example, if as a result of a debtor's act, a third party gained a material benefit to the detriment of the creditors, the creditors may demand that the act is declared ineffective. Therefore, when a company's solvency comes into question, the directors are required to act in the best interests of the company, without prejudicing or harming the creditors.

Polish law uses both the balance sheet test and the cash-flow test to determine whether or not a company is insolvent. Under the cash-flow test, a company is considered insolvent if it can not pay its debts when they fall due, whereas under the balance sheet test, a company is considered insolvent if its liabilities exceed the value of its assets. The tests are applied independently, i.e. even if the company is paying its debts as they fall due, it is considered insolvent if it fails to pass the balance sheet test, and vice versa.

According to Polish law, company directors are legally obliged to file for insolvency within two weeks of the day the company becomes insolvent. It is up to the directors to monitor the financial situation of the company on a constant basis and run the insolvency tests frequently enough to determine the moment when the company becomes insolvent. If the directors fail to comply with this obligation, they may face civil liability for any losses suffered by the company or its creditors, as well as criminal liability involving a fine, a penalty of restriction of liberty or up to one year's imprisonment. In practice, the most significant civil liability facing the directors of an insolvent company that fails to file for insolvency on time is liability for damage caused to creditors as a result of the delay (which is usually the difference between what a given creditor would have been able to recover if the insolvency filing had been made on time and what he actually managed to recover).

Polish law also imposes liability on the directors for the company's obligations if enforcement against the company (either by secured or non-secured creditors) is ineffective. There is a defence available to the directors if they file for bankruptcy or composition proceedings within the statutory time limits.

Additionally, directors are liable for actions detrimental to the company. This liability carries a penalty of imprisonment of up to five years and a fine.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	Polish law does not expressly prohibit creditors from extending credit facilities to a company in financial difficulties and leaves it to their discretion (although banks are under a legal obligation to verify the creditworthiness of borrowers and extend loans only to those entities which they consider creditworthy). However, the members of a lender's management board may face civil and criminal liability if it is proved that by extending credit to a borrower facing insolvency they caused damage to the lender (see the answer to question 1 for a description of the potential civil and criminal liability of the management board members). Such damage may be incurred by a lender if, for example, the extended credit facility (together with the accrued interest) is not repaid to the creditor due to the insolvency of the debtor. Therefore, if the risk of the borrower's insolvency is high, the members of the lender's management board should consider their own personal exposure.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	Polish law contains provisions enabling creditors to challenge certain transactions entered into in the period leading up to the date of insolvency proceedings, in particular: — Other creditors can seek to claim that such additional or extended security is ineffective or invalid, on the grounds that it is harmful to their interests, especially if the value of the security is significantly higher than the value of the loan it secures. — Creditors can challenge certain transactions entered into by an insolvent company with any of its shareholders, its representatives or their spouses, as well as with affiliated companies, their shareholders, its representatives or their spouses in the six month period preceding the filing of an insolvency application. — All transactions entered into by the company for no consideration, or where the value received by the company is considerably less than the value of the company's performance under the transaction, in the year preceding the filing of an insolvency application are ineffective. — The creation of a security interest by an insolvent company in order to secure an existing claim that is not yet due, which is entered into in the two-month period preceding the filing of an insolvency application, is ineffective. This does not apply to security granted in respect of a new debt.
4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Polish law does not expressly give creditors the right to appoint a director or observer to the board, or provide for any other direct method to monitor a company. Such monitoring is left to the contractual or business arrangements between the parties, and may take the form of reporting requirements or the obligation to allow representatives of the creditor access to company premises and documents, or giving the creditor the right to appoint its representative to a company's supervisory board.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Under Polish law it is possible to restructure a company's liabilities by converting receivable debts into shares if the borrower is not subject to insolvency proceedings. A debt for equity swap can sometimes also be achieved within the framework of composition proceedings. In either case, the company's shareholders' meeting should resolve to increase the company's share capital. The debt being exchanged is treated as a cash contribution. In some cases the consent of the President of the Office for Competition and Consumer Protection or other regulatory authorities may be required for the conversion of debt into equity.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	Generally, a settlement between a debtor and its creditors in Poland can only be binding on dissenting creditors if it is reached in composition insolvency proceedings. Under Polish law, if the requisite majority of a company's creditors agree to a debt restructuring in composition insolvency proceedings, the minority of dissenting creditors are bound by the majority's decision. However, such a settlement can only be reached in accordance with the rules and procedures of Polish insolvency law, which are, in part, designed to protect the interests of various groups of creditors. A settlement can be reached in most cases if a majority in number of creditors holding at least two thirds of the total amount of debt vote in its favour. However, under certain circumstances, the judge-commissioner may decide that creditors should vote in separate classes, according to their interests (for example employees, creditors who are secured with limited rights in rem on the assets of the debtor, creditors who are also shareholders of the debtor, etc.), and generally, the requisite majority must be achieved in all the creditor classes for the settlement to be approved. After the creditors have approved the settlement, it must also be approved by the court. The court will refuse to approve the settlement if the settlement breaches the law or if it is evident that the settlement will not be performed. The court may also refuse to approve the arrangement if its conditions are grossly detrimental to those creditors who have voted against the arrangement and raised objections. A settlement might be considered grossly detrimental to a certain creditor (or creditors) if the terms of the arrangement treat them unfairly compared to other creditors. If it is not possible to reach a consensual restructuring arrangement, the court will change the type of proceedings from composition insolvency to liquidation insolvency and appoint an insolvency estate trustee. If that happens, a consensual restructuring arrangement will no longer be an option. See the answer to question 7 below for more details about entry into a composition insolvency.
7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	Under Polish law there are two types of insolvency procedures: composition insolvency; and liquidation insolvency. Composition insolvency can be declared by the court when it is likely that the creditors will be better off under the terms of a settlement than if the debtor is liquidated. However, the court will not make an order for composition insolvency if evidence from the debtor's previous behaviour (such as wilful failure to execute court orders or comply with injunctions, or wilful misconduct towards creditors and bailiffs) shows that it is uncertain whether the debtor would comply with the terms of the settlement. A composition insolvency settlement usually takes the form of a debt reduction, although various forms of restructuring are possible (including the sale of the debtor's business as a going concern). After the settlement has been performed, the insolvent entity can continue normal operations (unless the terms of the settlement provide for the debtor's liquidation). Liquidation insolvency is declared when there are no grounds for declaring composition insolvency. All assets of the insolvent entity are sold (preferably by a sale of the entire business of the debtor) and the proceeds are distributed, in accordance with the order of priority prescribed by law. Once the insolvency proceedings end, the insolvent entity ceases to exist as a legal person.

DISTRESSED DEBT TRADING	
1. How does a lender sell a loan?	There are no specific requirements for the sale of a non-performing loan under Polish law. Therefore, general rules on the transfer of loans (and, in fact, any kind of receivables) apply, which means that they are usually transferred by way of assignment. Under the provisions of Polish law relating to the assignment of receivables, the transferor automatically warrants to the transferee the existence, validity and legal title of the receivable being assigned. The transferor sometimes also warrants the solvency of the debtor at the moment of the assignment. The debtor does not need to be notified of the assignment for the assignment to be valid. However, if the debtor is not aware of the assignment, it can effectively discharge its obligations by paying the assignor. The regulations on the assignment of receivables are not applicable to receivables under bearer documents nor to receivables under documents transferred by endorsement.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	Receivables secured by registered pledges and mortgages (which are registered in, respectively, the pledge register and the land and mortgage register) may only be transferred together with the corresponding pledge/mortgage. The pledge/ mortgage however is only transferred once the new pledgee/mortgagee is registered in the pledge register/land and mortgage register upon the new pledgee's/mortgagee's application to the appropriate registry court. This means that the secured receivable is not effectively transferred until the relevant registration is made. Most other typical forms of security (such as security assignments or security transfers of ownership) are generally not automatically transferred together with the secured receivable, and require a separate agreement in order to be transferred.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Apart from an assignment, the only way provided for in law by which a bank lender can off-load part of the risk or benefit in a loan, is securitisation by sub-participation, pursuant to which the loan receivables are sold to a "securitisation fund", which is a type of investment fund. There are no other specific regulations in Poland dealing with off-loading part of the risk or benefit of a loan. Arrangements of this type can be entered into on the basis of the general rules of Polish civil law, including freedom of contract, but they are not likely to have the regulatory, accounting and insolvency-related consequences usually desired by lenders.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	No licence or authorisation is required for the purchase or sale of non-performing loans. However, limitations on disposals of non-performing loans by banks may be applicable under banking secrecy regulations (see question 7 below) and securitisation regulations (see question 3 above).

5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	If a borrower buys its own debt, it has the same effect as if the debt were repaid: the debt is extinguished. There are no regulations specifically prohibiting or limiting the ability of companies associated with the borrower from buying debt owed by the borrower.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	Under Polish law, a creditor who acquires its claim after the declaration of the debtor's insolvency does not have the right to vote in relation to that claim, unless the transfer of debt occurs in connection with a legal relationship created before the declaration of insolvency. An example would be that of a corporate guarantor. A creditor that simply buys the insolvent company's debt after insolvency does not acquire the right to vote. The assignor of the debt also loses the right to vote in respect of it.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Under Polish banking secrecy regulations, a bank is generally not permitted to disclose any data regarding its customers without their prior written consent. It is widely accepted that such consent may not be general; it must specify an entity or entities to which the bank is allowed to disclose information. This makes trading in loan receivables by banks difficult. However, there are some exceptions. For example, banking secrecy restrictions do not apply to the extent required to enter into and perform agreements in connection with a securitisation transaction carried out pursuant to the securitisation rules (see question 3 above). Moreover, the customer's consent for the disclosure of its data is not required when selling loans which, for accounting purposes, have been classified by the bank as written-off, and when selling loans to other Polish or EU banks. Please note that, according to some opinions, the transfer of consumer loan receivables without the borrower's consent may be treated as a so-called abusive practice under Polish consumer protection laws. A way of mitigating this risk would be to obtain the borrower's deemed consent for the transfer of the loan. (e.g. by sending to the customers, along with one of the periodic statements from the bank that they receive, a notice giving them the option to oppose to the transfer of their loan within a certain deadline).

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FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

The Romanian company legislation provides that directors must manage the company with prudence and loyalty, in the company's best interests. This duty continues to apply where the company suffers financial difficulties. The directors of an insolvent company may be held liable if it can be proved that they have not acted in the best interests of the insolvent company, and there are additional liabilities for fraud.

Directors of a distressed company are advised to seek professional advice and keep the shareholders informed about the company's financial status and potential future risks.

The Romanian Company Law requires that, if the company suffers losses (calculated on the basis of the annual financial statements) to the extent that the value of the net assets (calculated as the difference between its total assets and its total liabilities) is reduced to less than half the value of the subscribed share capital, the directors must convene a general meeting of shareholders immediately, in order to decide on the dissolution of the company.

A debtor is considered "insolvent" when it cannot pay a debt that is for a sum certain, due and payable. Insolvency is presumed if debts remain unpaid for more than 90 days from the date when they became due and payable. Insolvency is "imminent" when it is determined that the debtor will not be able to discharge its debts when they become due and payable in the future.

An insolvent company is required to file for insolvency proceedings with the court within 30 days from the date of onset of presumed insolvency. When insolvency is "imminent", the company may, but is not obliged to, file a request with the court to enter insolvency proceedings.

A legal representative of an insolvent company (i.e. a director with powers of representation of the company) who fails to file a request within six months from the date when he should have applied for the company to be put into insolvency proceedings may be subject to criminal liability.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	Yes. There are no express provisions under Romanian law preventing a Romanian lender from extending existing loans to a borrower in financial difficulty. Under recent amendments to Romanian insolvency legislation, the initiation of insolvency proceedings does not automatically terminate ongoing contracts (i.e. contracts that have not been completely or substantially performed by either the insolvent company or any of its counterparties). Any contractual clauses triggering the termination of such contracts as a result of insolvency proceedings are void. As the judicial administrator or the judicial liquidator has to ensure that the value of the insolvent company's assets is maximised, they are vested with powers to decide whether a particular ongoing agreement is to be terminated or not. In the light of these new amendments, it is possible that ongoing loan facilities (i.e. facilities that have not been fully or substantially drawn down at the time the insolvency proceedings are initiated) may survive the initiation of insolvency proceedings if the judicial administrator or liquidator wishes to continue them, but usually on renegotiated terms acceptable to both lender and judicial administrator or liquidator. If the proceedings continue after the observation phase, the judicial administrator or the judicial liquidator may terminate such loans without lender's consent provided that the termination increases the insolvent company's assets.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	Any new or extended security created in the three year period prior to the opening of insolvency proceedings may be challenged by the insolvency officials or other creditors, if it is determined that the transaction was made with the purpose of preferring one creditor over others or if it is deemed a transaction at undervalue. In addition, if an unsecured creditor is granted any real security (such as a mortgage or a security interest on movable assets) within a period of 120 days prior to the opening of insolvency proceedings, the giving of such security may be challenged by the relevant insolvency officials and could be set aside by court order. By way of exception, certain agreements made between the insolvent debtor and its lenders as part of a debt restructuring scheme (including a pre-insolvency work out plan) cannot be challenged by insolvency officials. To fall within this exception, these agreements must be capable of restoring the financial standing of the insolvent company and must not be made with a view to defrauding (or otherwise prejudicing) the other creditors of the debtor.

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Prior to the commencement of insolvency proceedings a lender does not have any rights to appoint a director to the borrower, regardless of the size of the debt. Only the borrower's shareholders have power to appoint (or terminate the appointment of) directors. Contractually, the lender may be granted certain rights in this respect, subject to shareholders' consent. There are no statutory means to appoint a director as an observer other than by contractual arrangements with the borrower and its shareholders. Such a provision is not uncommon in loan agreements, but it is not yet a general practice in Romania. A creditor filing a request for the opening of insolvency proceedings can simultaneously request the appointment of a judicial administrator (although the identity of the administrator is subject to confirmation by court). Unless the creditor filing the request holds more than 50% of the company's debt, the appointment of such judicial administrator has to be confirmed by the creditors meeting. Following the commencement of insolvency proceedings, the lender can monitor and control the company as a member of the creditors' committee. Membership of the creditors' committee is usually decided by the general meeting of creditors, which elects 3 or 5 committee members from among the first 20 creditors, ranked in the order of the value of their claims against the company. The creditors' committee has various powers to assist and monitor the judicial administrator or liquidator.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Romanian Law allows a company to increase its share capital by means of converting some or all of its due and payable debts into equity. The corresponding increase in share capital needs to be approved at a shareholders' general meeting. If the company is listed, there are certain formalities that need to be complied with and there could also be certain obligations imposed on the creditor that is converting its debt into equity. There are limits on the percentage shareholding that a Romanian credit institution can hold in a company whose scope of activity is not related to financing activities, except for the purposes of restructuring. A creditor should also be aware that by participating in a debt for equity exchange, it would lose any security rights attached to the debt.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	A company that faces imminent insolvency may agree with its creditors the terms of a restructuring by way of a work out plan (*"concordat"*). A work out plan is presented for approval to the company's creditors. The plan is passed on the approval of creditors holding at least two thirds of the claims that the company has either accepted or not contested. If the plan is approved by creditors, it will be endorsed by the court. In addition, the court can, amongst other things, postpone dissenting creditors' claims by up to 18 months on certain conditions or order a stay of enforcement against the distressed company, including enforcement proceedings brought by dissenting creditors. The dissenting creditors do, however, have available procedural means to resist such measures. If insolvency proceedings have already been commenced, creditors holding at least 20% of the company's claims or the judicial administrator may formulate a reorganisation plan. The reorganisation plan must first be sanctioned by the court and then approved by the creditors' meeting, which is divided, for voting purposes, into categories of creditors according to type of claim (for example: secured claims, key unsecured creditors, other unsecured creditors, employees and the state). A category of creditors approves a reorganisation plan if an absolute majority in value of claims in that category accepts the plan.

A reorganisation plan is approved upon the following conditions being jointly met:

(i) a majority of non-disadvantaged categories, and (if there are any) at least one disadvantaged category of creditors (determined by value) accept (or are deemed to have accepted) the plan;

(ii) the plan provides for fair and equitable treatment of each disadvantaged claim and

(iii) the plan meets all formal requirements set out in the Insolvency Law. Generally, a claim is presumed disadvantaged if the reorganisation plan provides for a reduction in the amount of that claim, or for the reduction of the security or other rights supporting that claim.

If there are only two categories of claims in the payment schedule, the plan is deemed to be accepted if the category with the highest total value of claims has accepted the plan. Following approval of the court, the reorganisation plan comes into force and the debtor's business is restructured accordingly. The claims and rights of the creditors and the other parties concerned are modified as provided for in the plan.

If the company does not comply with the plan or if further losses are incurred, the judicial administrator, the committee of creditors or any of the creditors, as well as the special administrator may apply to court at any time to approve commencement of bankruptcy proceedings. If no reorganisation plan is approved, the court orders the immediate commencement of bankruptcy proceedings in respect of the debtor.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?

An insolvent company may continue trading either while attempting to agree a pre-insolvency work out plan or during the reorganisation procedure, if insolvency proceedings have already been initiated.

During a pre-insolvency work out plan a company is still entitled to run its business subject to the terms of the plan. Any sale of the company's assets or business in the course of a pre-insolvency work out plan needs to be effected in accordance with the plan and with the consent and co-operation of any secured creditor. (Pledged movable assets can be sold without the secured creditors' consent, but the pledged assets would be transferred subject to the security interest, which usually makes such a sale undesirable.)

Throughout a reorganisation procedure, the company's business is managed by a special administrator, under the supervision of a judicial administrator. The shareholders do not have the right to interfere in the management of the business or in the administration of the company's property, except for and within the limits expressly and restrictively provided by law and the reorganisation plan. A reorganisation plan can take the form of one (or more) of the following: a business restructuring, a financial restructuring or a sale of assets.

DISTRESSED DEBT TRADING	
1. How does a lender sell a loan?	The two most common means of transferring rights and/or obligations attached to a loan in Romanian Law are assignment and novation. An assignment transfers rights but not obligations. A valid assignment of rights does not require the consent of the relevant counterparty (i.e. the debtor), however, the creditor's obligations under the assignment are only enforceable if a notice of the assignment is sent to the debtor. Under the assignment, the rights or receivables are transferred to the assignee together with all the ancillary rights of the assignor (including any security interests attached to the relevant right or receivable). Novation is a legal mechanism for modifying an obligation. By means of a novation either the creditor or the debtor could be replaced or the obligation itself can be modified (without changing the parties). Where a novation is used, the original obligation is terminated and a new obligation is created. This means new 'hardening periods' start from the novation date in respect of security. In addition to that, the debtor of the obligation being novated must consent to the novation. Importantly, agreements for the extension of existing security and/or creation of new security that are part of a debt restructuring scheme (including an insolvency work out plan) are exempted from hardening periods. In order for this exemption to apply, such agreements (i) must be capable of restoring the financial standing of the insolvent company and (ii) must not be entered into with a view to defrauding (or otherwise prejudicing the other creditors of that insolvent company. The usual method of transferring a non-performing loan is that the existing lender and the new lender enter into a transfer agreement, which incorporates both an assignment of rights and a novation of the existing lender's obligations under the loan agreement. The borrower must be a party to the transfer agreement, so that the novation is legally effective (however, there are ways of avoiding the need to seek the borrower's consent, such as pre-agreeing the transfer mechanism, etc.).
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	In the case of an assignment of rights or receivables, security interests are transferred to the assignee by operation of law. In the case of a novation, the transfer of security created to secure an obligation that is being novated would only take place if the parties expressly agreed. Usually the new lender will want to enter into addenda to the security documents in order to become a party to such documents and to complete all the ancillary formalities (such as registrations with various public registries).
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Romanian Law does not expressly prohibit sub-participation, and it is possible (and fairly common) to set up a sub-participation structure where a sub-participating lender assumes the benefits and the risks associated with a loan granted by the lender of record. However, such a structure raises regulatory and accounting issues for banks, some of which are more comfortable with transfer structures as a result.

4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignee or the borrower?	Assuming that the original lender is a financial institution, if a non-performing loan is transferred as a whole (i.e. all rights and obligations are transferred from the existing lender to a new lender), the new lender would have to be a (regulated) financial institution as well, because under Romanian law, providing credit on a professional (regular) basis is allowed only if the provider of credit is a credit institution or a non-banking financial institution. However, if the existing lender only attempts to assign the receivables to a third party in order to remove the unpaid debt from its balance sheet (by way of a sub-participation structure), the assignee would not have to be a financial institution, it could be any entity acting within the scope of its activity (e.g. a debt recovery company).
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	There is no provision under Romanian law that prohibits the transfer of any part of the receivables payable by the borrower to an affiliate of the borrower, by one or more of the existing lenders. If the borrower itself were the purchaser, the debt would be extinguished.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	In Romania, this depends on whether a definitive schedule of claims has been approved by the court. If the transfer occurs after the opening of the insolvency procedure but before the definitive schedule of claims is approved by the court, the acquiring party will be able to vote provided the transfer is valid and the claim and transfer is duly recorded in the schedule of claims. Conversely, if the transfer occurs following the opening of the insolvency procedure and after the definitive schedule of claims is approved, it is ambiguous whether the acquirer can vote. There are arguments both ways.
7. Are there any data protection or confidentiality issues in your jurisdiction that would hinder or prevent a lender from selling and/or transferring loans?	There are both confidentiality and data protection issues that need to be taken into account by a Romanian credit institution when considering the transfer of its exposure under a loan to other entities. It is therefore advisable and often necessary for credit institutions to make contractual provision in the loan documentation allowing them to disclose and transfer confidential information to a (potential) purchaser.

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FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

A Russian company can, but is not obliged to, make an anticipatory application for insolvency if it meets certain debt criteria (based on the amount and term of the debt) and it forecasts insolvency.

Under Russian law, a chief executive officer (or general director, referred to as the "CEO") is obliged to file for insolvency in a number of circumstances, including:

(i) where the company is unable to pay creditors;
(ii) where the company is subject to an enforcement action against its assets that prevents it from continuing its operations;
(iii) where the company's liabilities exceed its assets; or
(iv) when a decision is taken by persons authorised by the company, or the company's owner, to apply for insolvency.

The CEO must file for insolvency within one month of the relevant circumstance arising. Failure to do so may lead to the CEO incurring personal liability under insolvency law for potentially all unsatisfied financial obligations of the company that may arise following the expiry of that one-month period.

In addition to civil liability, if the CEO fails to file an insolvency petition when required, it will give rise to an administrative liability. This can result in a fine of up to an equivalent of approximately USD 300 or disqualification of the CEO from holding any managerial positions in any company for up to two years.

Except for the ultimate obligation of a CEO to file for insolvency, Russian law does not prescribe actions of the board of directors (being a supervisory management body under Russian law) in circumstances where the company is in financial difficulties. Neither does it impose any express duty on the CEO to have regard to the company's creditors rather than its shareholders in an insolvency situation.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?

Yes. Russian law contains no legal restrictions on granting credit facilities to a company in financial difficulties. However, once insolvency proceedings have started, obtaining credit facilities is subject to the relevant administrator's consent or to the creditors' committees' approval (depending on the phase of insolvency and, in the case of the external administration, the terms of the plan of external administration (please see the answer to question 7 below for more information about external administration)).

3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?

There are no provisions in Russian law restricting creditors from offering support conditional on additional or extended guarantees and/or asset security. However, because a CEO must not prefer one creditor (or class of creditors) to another, such security might be vulnerable to challenge. Russian insolvency law states that a court may declare transactions invalid if they result in one creditor's claims being prioritised over another. A transaction is a preference if it:

- involves granting security to an existing creditor to secure obligations that arose prior to the transaction;
- has or may result in a change of ranking in which the existing creditors' claims are satisfied;
- has or may result in the satisfaction of claims that have not yet matured, provided there are other unsatisfied but due claims; or
- results in one creditor's claims, which arose prior to the transaction, being prioritised over other creditors' claims.

For the challenge to succeed the transaction must:

- give a preference to an existing creditor as described above; and
- have been completed during one month before, or at any time after, the initiation of bankruptcy proceedings against the debtor; or
- have been completed within the six months prior to the initiation of bankruptcy proceedings against the debtor provided that either:
  - (a) the transaction provides security to an existing creditor and has or may result in a change to the priorities in which the existing creditor's claims are satisfied; or
  - (b) the creditor or another party involved was aware that the debtor met the inability to pay and/or the asset insufficiency criteria.

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?

Before the company enters an insolvency process, additional monitoring by a lender is only possible if the loan agreement contains relevant contractual provisions. If this is not the case, the lender has no statutory right under Russian law to appoint a CEO or a member of the board of directors.

If the company is in initial insolvency proceedings (such as supervision or financial rehabilitation – see the answer to question 7 below for more explanation of these terms) the lender still has no power to appoint a new CEO, but it can monitor the company by being part of the creditors' committee. Creditors' committee members are entitled to request any information on the debtor from the administrator.

If the company is in full insolvency proceedings (external administration or liquidation (see the answer to question 7 for an explanation of these terms) the CEO is replaced by an external administrator or a liquidator, who is chosen by the creditors. The creditor's committee keep their right to ask for any information on the debtor from the administrator. Moreover the administrator is obliged to report to the creditor's committee on progress in implementing the external administration plan and to present to the creditors' meeting, at the end of the external administration procedure, a report on the results of external administration, which should include details of the debtor's financials.

5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Following recent changes to Russian corporate law, debt to equity exchanges are now permitted in Russia. The law now recognises that a shareholder or participant's "right of claim" may be set off against its obligation to pay its charter capital contribution to the company. Subject to exceeding certain thresholds (in relation to the size of an acquisition and/or the size of the company), an acquisition of shares or participatory interests may require prior consent from, or post acquisition notification to, the Russian anti-monopoly authority. Additional requirements have been established by the federal executive body responsible for the securities market with regard to the acquisition of shares in a joint stock company. Equity acquisition in a closed joint stock company and a limited liability company is also subject to pre-emption rights and limitations on transfer established in the company's charter. Following the commencement of bankruptcy proceedings, the exchange of creditors' claims for corporate rights in the debtor is possible only through a voluntary arrangement.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	Prior to the commencement of bankruptcy proceedings, a debtor can agree a debt restructuring with a particular creditor (or creditors) that will only affect the particular creditor's debt. It cannot bind other creditors without their consent, and the majority creditors cannot compel the minority creditors to agree a debt restructuring. Following the commencement of bankruptcy proceedings, debt restructuring is possible using a voluntary arrangement. A voluntary arrangement must be approved by a majority of the creditors voting at a creditors' meeting of all creditors in the register of the debtor. All secured creditors must vote in favour of the voluntary arrangement for it to be approved. A voluntary arrangement is effective from the moment of its approval by the court. The voluntary arrangement must not treat minority dissenting creditors, or creditors that did not participate in the voting unfairly. If this rule is not observed, the voluntary arrangement may be challenged in court by an affected creditor and subsequently terminated.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?

Any consensual deal with creditors of a company that is in financial difficulties is subject to Russian insolvency (bankruptcy) law requirements. Once bankruptcy proceedings are initiated against the company, any transactions entered into by the company during a certain period (from one (1) month to three (3) years) preceding the bankruptcy filing, may be invalidated by a court if it is proven that the transaction is a "suspicious transaction" or a "preferential transaction".

The following bankruptcy procedures aim to restore the debtor's solvency and arrange for outstanding debt to be discharged:

— Financial rehabilitation: the aim of this procedure is to rescue the company through the repayment of debt in accordance with the court approved financial rehabilitation plan.
— External administration: this insolvency procedure provides for the management of the debtor's assets and the taking of an inventory by an administrator, whose powers include (i) closing unprofitable production facilities; (ii) selling portions of the debtor's business or property; and (iii) increasing the authorised share capital by way of floating additional ordinary shares.

Apart from the procedures listed above, Russian insolvency law also provides for the following procedures:

— Supervision: the key aims of this (initial) procedure are: (i) to analyse the debtor's current financial status and draw up a register of creditors' claims, and (ii) to preserve the debtor's property by restricting the debtor's and its management's actions.
— Liquidation: this (final) procedure focuses on the realisation and distribution of the debtor's assets and may be instituted for a period of six months (with a six month extension). In this procedure, the winding-up of the debtor is carried out.
— Voluntary arrangement: please see the answer to 6 above for information on voluntary arrangements.

As a general rule, a company is entitled to continue to trade (with certain limitations and with the knowledge of the administrator) during the following bankruptcy proceedings: supervision, financial rehabilitation and external administration. If a company goes into liquidation the company's business activities cease.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?

Under Russian law the most common mechanism of debt transfer is assignment. Assignment is the transfer of the lender's right (the claim) to another person. Unless otherwise stipulated by law (e.g. the transfer of rights to a surety who has fulfilled obligations of a debtor and has thus acquired the rights of the primary lender) or by agreement, the rights of the primary lender are transferred to the new lender within the scope and on the terms existing at the time of the transfer of those rights. To effect an assignment, the consent of the debtor is not required, unless otherwise stipulated by law or by agreement.

Novation under Russian law involves the termination and replacement of an obligation by agreement between the parties. The primary obligation is replaced with a new obligation between the same persons and a different object or a different way of discharge is stipulated. Therefore, novation under Russian law cannot be used for debt trading.

2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	Unless otherwise stipulated by law (e.g. the transfer of rights to a surety who has fulfilled obligations of a debtor and has thus acquired the rights of the primary creditor) or by agreement, any related security rights of the primary creditor are automatically included in the assignment of a loan to a new creditor. Transfers of certain types of security (such as mortgages and share pledges) require additional registration with regulatory authorities.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Russian law does not prohibit structuring sub-participation arrangements either on a funded or unfunded basis, and in practice arrangements that utilise the Russian concept of "guarantee deposits" (*garantiyniy deposit*) are widely used for this purpose. A guarantee deposit structure typically utilizes an arrangement whereby a sub-participant opens a deposit account in a bank-creditor to purchase (or fund) a sub-participation. In doing so the sub-participant accepts the risk of non-performance of the loan and deposits an amount that will be available to the bank-creditor if the loan is not repaid. The sub-participant should be able to withdraw the interest from the deposit account accrued on the amount deposited. If the loan is repaid the sub-participant recovers the deposited amount in full. Otherwise the bank-creditor withdraws the deposited amount to repay the outstanding amount of the loan. Unfunded arrangements are also entered into. In this context a guarantee is typically procured by a company from a third party, which is deposited with the bank-creditor, and which guarantees under a suretyship agreement the performance of the obligations of an unfunded sub-participant. In case of default the surety repays the amount of the sub-participant's obligations to the bank-creditor. Thereafter the surety substitutes the bank-creditor and acquires the rights of recourse to the sub-participant to repay the amount paid by the surety to the bank. Any guarantee deposit agreement must comply with the relevant requirements in the Civil Code of the Russian Federation.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	A transfer of a non-performing loan does not qualify as the provision of banking or financial services and therefore no licence or prior regulatory authorisation is required.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	Russian law does not expressly prohibit a borrower, or a company associated with the borrower, from buying part of the debt that it owes to (a) lender(s). However, any debt buy back by the borrower will be treated under Russian law as a repayment with discount. This leads to certain negative tax consequences for both the borrower and the lender. If a borrower buys all of the debt it owes to a lender or lenders, the loan is extinguished.

6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	Under Russian law creditors whose claims arose before the filing of a bankruptcy petition and which are included in the register, can vote at creditors' meetings. For certain types of obligations arising under continuing agreements (e.g. under power supply agreements) the date these obligations arose is crucial. Those arising before the filing of a bankruptcy petition will give rise to voting rights, and obligations arising after the filing of a bankruptcy petition will be current claims (without voting rights). If, after commencement of insolvency proceedings, a person acquires debt from an existing creditor, the new creditor will have the same rights as the former creditor (including voting rights).
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Russian law requires creditors to keep confidential any information concerning their clients and the essential terms of all agreements. This information can only be provided to the Credit Reference Bureau with the prior consent of the relevant borrower. If the loan documentation does not expressly allow disclosure to third parties then the borrower's prior consent will be required.

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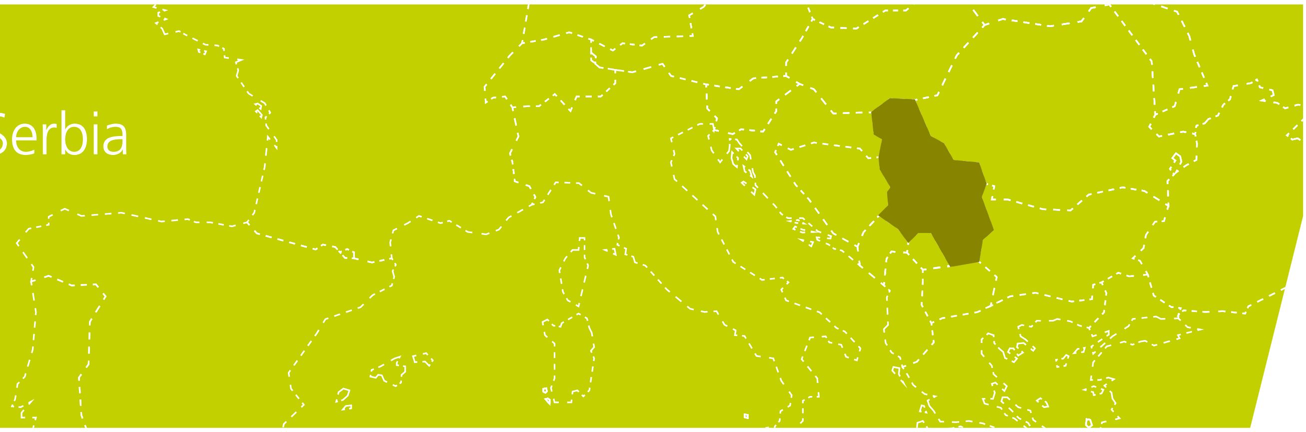

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

Members of the board of directors and of the managing board and any persons engaged in the management of the company owe general duty of care and loyalty to the company and are subject to a corresponding liability for breach of any of these duties.

The directors' and officers' overriding duties are to carry out their functions in good faith, with the care of prudent businessmen, and in the reasonable belief that they are acting in the company's best interests.

Failure to comply with these duties can lead to personal liability to the company. If, in making business decisions, directors rely on professional advice they are not held liable for damages to the company which may arise from those decisions.

Serbian law does not formally require directors to file for insolvency but the directors' conduct in the period starting from the discovery of financial problems and ending with bankruptcy proceedings is subject to scrutiny during the bankruptcy procedure (please see the answer to Q3 below).

The law imposes criminal liability on a director who causes financial loss or insolvency to the company and this can result in personal liability to the company for the damage caused by the financial loss and insolvency.

The law does not prescribe any specific measures that directors of a company facing financial difficulties have to take; however, they are required to maintain the company's charter capital above a minimum value. If the company's minimum charter capital falls below EUR 500 for a limited liability company, EUR 10,000 for a closed joint stock company and EUR 25,000 for an open joint stock company, the company must increase it to the required level within six months. If the company does not comply with this requirement, a liquidation proceeding must be initiated. Directors can be fined for failure to maintain the minimum charter capital requirement.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	There are no express restrictions on creditors extending credit facilities to a company in financial difficulties. However, certain transactions entered into by the company in a prescribed period before the insolvency proceedings begin can be subsequently challenged (please see the answer to Q3 below). The criminal liability (referred to above in the answer to Q1) of a company's responsible person causing financial loss to that entity may apply indirectly to a creditor's responsible person where that creditor grants a loan to an already insolvent debtor and in that manner causes financial loss to other creditors. If insolvency proceedings have already commenced, the bankruptcy administrator may, with the approval of the creditors' committee, enter into loan facility agreements and related security agreements on behalf of the company in order to keep the company operating. Such loans are treated as expenses of the insolvency proceedings and enjoy priority in the distribution of insolvency proceeds, ranking ahead of employment and tax liabilities and other creditors.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	All securities acquired through enforcement proceedings or newly created security within 60 days before the start of bankruptcy proceedings are void. In addition, other transactions that completed before bankruptcy proceedings but which interfere with the pari passu principle, or are damaging to creditors, or place one or more creditors in a better position than other creditors, may be avoided if challenged either by the bankruptcy administrator on behalf of the debtor, or by creditors: (a) Congruent settlement: Legal transactions and actions entered into within six months before filing for bankruptcy proceedings, which provide security or settlement to a creditor, may be contested if the debtor was insolvent at the time and the creditor knew or ought to have known of debtor's insolvency. (b) Incongruent settlement: Legal transactions and actions that provide security or settlement for one creditor, which it was not entitled to request, or which it was entitled to request but not in the manner and at the time when it was provided, may be contested if the transaction was entered into within twelve months before filing for bankruptcy proceedings. (c) Directly detrimental legal transactions: Legal transactions entered into within six months before commencement of bankruptcy proceeding that are directly damaging to the creditors may be contested (among other reasons) if the debtor was insolvent at that time and the counterparty knew of the debtor's insolvency. (d) Intentionally within five years before filing for bankruptcy proceedings detrimental legal transactions: Legal transactions or actions entered into or taken with the intention of causing damage to one or more creditors may be contested, if the counterparty knew of the debtor's intention. Knowledge of intent is presumed if the debtor's counterparty knew that there was a threat of insolvency against the debtor and that the action would damage the bankruptcy creditors. (e) Transactions and actions with no, or negligible, compensation: legal transactions and actions of the bankrupt debtor that are entered into within five years before filing for bankruptcy proceedings either for no compensation or for a negligible compensation may be contested.

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	There is no provision in Serbian law that entitles a lender to monitor a distressed debtor that is not yet subject to insolvency proceedings more closely, but contractual terms can be agreed. However, lenders may appoint a director or a member of the board of directors of the company if the company's shareholders so resolve. The lender appointee is then subject to the same duties and obligations as any other director or member of the board of directors (please see the answer to Q1 above). During insolvency proceedings, lenders may monitor the company more closely. Lenders (together with other creditors) have the right to vote at a creditors' meeting based on the value of their claims. The creditors' meeting must appoint a creditors' committee consisting of at least three, but not more than nine members. The creditors' committee can exercise certain powers over the bankruptcy administrator and the company including giving an opinion to the bankruptcy administrator about the manner of sale of the company's assets, approving entering into a loan agreement by the company and obtaining access to the company books and other documents.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Serbian law permits debt for equity conversion, but only in the case of limited liability companies. The process works as follows: first, the corporate body of the company decides to increase the company's equity capital by converting debt. If the relevant creditor is a third party (rather than an existing shareholder), then the company would have to amend both the articles of association and the shareholders' agreement. If the creditor is an existing shareholder then only the articles of association have to be amended. In order to register the increase of capital in these circumstances, the company has to submit proof of the existence of the debt to be converted to the Commercial Registry. The increase of capital through debt to equity conversion can then be registered and finalised.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	There is no mechanism in Serbian law that permits the majority creditors to compel the minority dissenting creditors to agree to a debt restructuring. The opposite is possible however: if, at the creditors' hearing in bankruptcy proceedings, creditors who hold 70% or more of the debt decide for bankruptcy of the debtor instead of restructuring, the bankruptcy judge may decide to proceed with a mandatory sale of the debtor's assets.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?

Under the Bankruptcy Act in Serbia a company can be made the subject of reorganisation or bankruptcy proceedings.

The reorganisation procedure allows the company to continue operating in the ordinary course of business while negotiating a consensual deal with its creditors aimed either at the company's survival or the sale of its business. The reorganisation plan may suggest a wide range of solutions, including, for example: debt reduction, debt for equity swap, financial or equity restructuring, or the sale of some or all the company's business or assets.

Once the company's debts and existing assets are determined, the bankruptcy administrator can formulate a reorganisation plan, which determines exactly how the company's debt will be restructured, with the intention of securing the company's survival and avoiding the bankruptcy procedure.

Alternatively, the reorganisation plan can be proposed by the bankruptcy debtor, creditors holding at least 30% of secured liabilities, bankruptcy creditors holding at least 30% of unsecured liabilities or persons holding at least 30% of the bankruptcy debtor's capital.

In order for a reorganisation plan to be adopted, each creditor class has to adopt it separately pursuant to a simple majority vote except for any class of creditors that is to be paid in full. Once a reorganisation plan has been adopted by the creditors, the bankruptcy judge approves it if the plan is in accordance with the provisions of the Bankruptcy Act. However, if at the bankruptcy creditors' assembly, 70% of creditors vote for the debtors' assets to be liquidated, the bankruptcy judge will order the sale and the reorganisation plan cannot proceed.

If the consensual deal cannot be achieved, an orderly sale of the company's assets or business for as much money as possible can be achieved in a bankruptcy procedure.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?

Serbian law prescribes a procedure for the transfer of any claim, unless the claim is non-transferable. Claims are non-transferable if:

(i) there is a non-assignment clause in the underlying agreement;
(ii) the law so provides; or
(iii) the claim is personal in nature and cannot be transferred to another person.

For the valid transfer of a transferable debt, the debtor must be notified, but need not consent, except where the transferee is a non-Serbian lender. If a notification is not made, the debtor may repay the transferor and obtain a valid discharge; the transferee would have no rights against the debtor in that scenario.

In addition, the National Bank of Serbia issued a binding opinion that only banks are entitled to buy loans because the Banking Act stipulates that only entities with a banking licence may engage in credit activities. However this prohibition only applies to Serbian transferees.

The transfer of a cross-border loan between a non-resident lender and a Serbian borrower can only be transferred to another non-resident lender (as transferee) and, as referred to above, requires the consent of the Serbian borrower.

2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	All forms of security (mortgage, pledge, contractual penalties, guarantees, interest rates, etc) follow the main debt and transfer to the transferee. However, where the security is possessory, the actual asset that is subject to the security right stays in the possession of the transferor, who holds it in the name, and for the account of, the transferee.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Sub-participation agreements are allowed under Serbian law, and other risk-sharing procedures may be available, depending on the circumstances. Sub-participation is effected by an agreement between the existing lender and the sub-participant whereby the sub-participant assumes the benefits and risks associated with a loan granted by the existing lender. This means that the sub-participation does not affect the relationship between the original lender and debtor, and that the existing original lender remains liable to the debtor for obligations contained in the underlying credit agreement. In the sub-participation arrangement, the ancillary rights and securities are not assigned to the sub-participant, due to the fact that the sub-participation arrangement only creates a personal obligation between the existing lender and sub-participant.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	In order to purchase, sell or collect debts in Serbia, a banking licence is required. However, no additional specific regulatory authorisation is required in relation to non-performing loans.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	Serbian law permits the borrower (or a company associated with the borrower) to buy its debt from the lender. That purchase is then treated as discharge of the borrower's obligations. As a principle of contractual freedom, the borrower may also agree with the lender to buy its own debt at a reduced price. However, there are special rules when there is a legal relationship with a foreign element. In practice, these rules make it legally impossible for a foreign company to take over the debt of a domestic company and vice versa.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	A bankruptcy creditor is defined as a person who has an unsecured claim against the debtor on the date of the commencement of the bankruptcy procedure. These bankruptcy creditors become members of the creditors' meeting, which decides (among other things) on the sale of the debtor's assets. Therefore, a person who takes over a debt after the start of the bankruptcy procedure will have no voting rights, because it is not a member of the creditors' meeting (and the initial creditor would also lose its voting rights after transferring its interest). A secured creditor does not count as a bankruptcy creditor (except in relation to any unsecured shortfall) because its claim will be settled with whatever form of security it has; it therefore has no right to influence the bankruptcy procedure.

7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Data relating to the fulfilment of a borrower's obligations to a bank is excluded from the list of confidential data subject to data protection. Consequently, a debtor who is already in default cannot object to the transfer of its data in connection with the sale of its non-performing loan.

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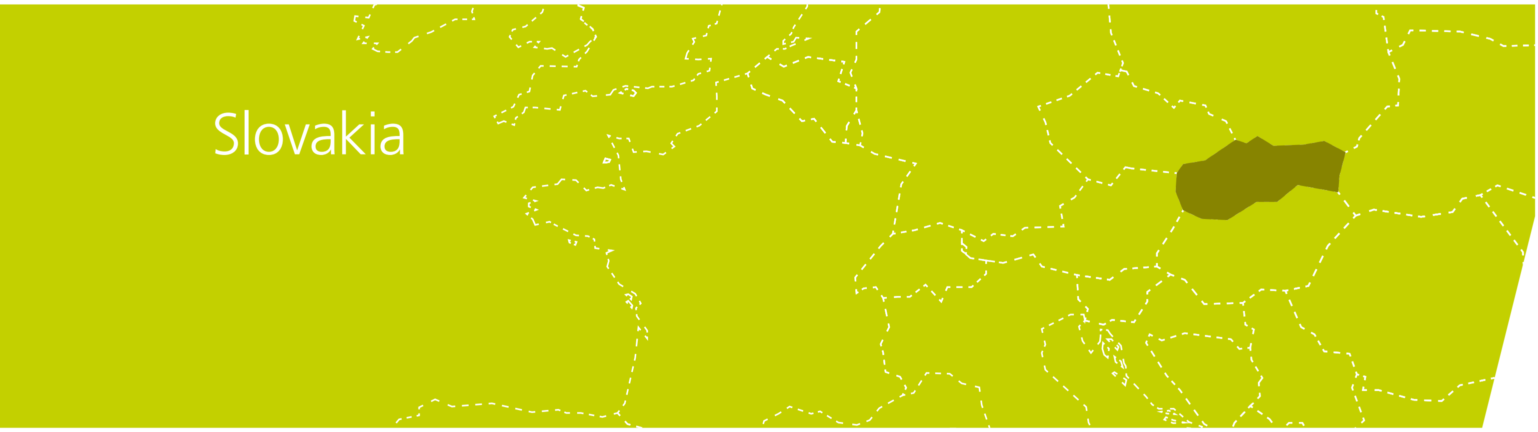

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

Under Slovak law debtors are obliged to continuously monitor their financial status, and their assets' and liabilities' balances. Diligent performance of this obligation enables early identification of any threat of insolvency and allows the debtor time to adopt appropriate measures.

Measures of this type are not expressly defined by Slovak legislation, but they can include increasing the equity by issuing new stock, closing down unprofitable operations, optimising the maturity of loans accepted, or issuance of debentures, stock reduction and optimising maturity of receivables and obligations. An appropriate and highly efficient measure to avert impending insolvency is to agree an informal restructuring of the undertaking with the creditors. This is the least stressful solution, as it provides the debtor with a chance of survival, it protects shareholder contributions, and usually provides for full creditor satisfaction. However, an informal restructuring takes time to put in place, and so if the debtor leaves it too late, there may not be time to put an informal restructuring together before the obligation to file for insolvency arises (see below).

The statutory body of a debtor (or members of its statutory body) must file for insolvency proceedings within 30 days of the date when they knew (or ought to have known) of the debtor's impending insolvency. Failure to comply with this obligation can result in personal liability for the members of the statutory body to creditors in respect of their unsatisfied claims. Liability for damages resulting from late filing for insolvency proceedings are evaluated in direct connection to the debtor's obligation to continuously monitor its financial status and its assets and liabilities.

In Slovak law, a debtor is insolvent if

- (i) it has more than one creditor; and
- (ii) more than one financial obligation has been due for more than 30 days (the "liquidity test");

or if it is over-indebted i.e.

- (i) it has more than one creditor; and
- (ii) its due financial obligations exceed the value of its financial assets (the "balance sheet test").

When a debtor is insolvent, it can either file for insolvency or file for restructuring approval.

If a debtor decides to opt for restructuring approval, an administrator must be appointed, who must prepare a report for the court on the feasibility of the restructuring. After the bankruptcy petition opening the insolvency proceedings has been filed with the court, the debtor may apply for a stay on the insolvency proceedings, as long as the court has not yet declared the debtor bankrupt. The stay lasts for a period of 30 days, and allows the debtor to prepare the filing for restructuring approval.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	There are no express restrictions limiting a creditor's ability to extend credit to a company in financial difficulties, but if a creditor is aware of the adverse financial status of a debtor, it should carefully evaluate whether the debtor will be able to repay both the existing and the extended facility. Unlike in some other jurisdictions, in Slovakia, a lender is not at risk of incurring liability to other creditors by extending facilities to a distressed borrower.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	The court can declare that certain acts that occurred within one year (or three years if the beneficiary of the voidable act is a related person) before the insolvency order has been issued, are ineffective (voidable acts). Contestable acts are: (i) legal acts entered into without reasonable consideration; (ii) legal acts amounting to preferential treatment of one of the creditors; (iii) detrimental legal acts; and (iv) legal acts made after rescission of the insolvency proceedings if within six months thereafter the debtor was again declared bankrupt. So, for example, if a company enters into a new security document before insolvency proceedings start, the purpose of which is to secure the company's existing obligation by encumbering the company's assets or property, such a security agreement would be considered a preferential transaction (i.e. a transaction that grants one creditor's debt more advantages than other creditors') and would be vulnerable to challenge as a voidable act. Creditors and/or the trustee (who is the person appointed by the court to administer the bankrupt's assets) can bring an action within six months after the court has issued the insolvency order for a declaration that such acts are ineffective.
4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	A lender's options to monitor the activities of the debtor are not expressed in or limited by legislation, but are usually defined in credit agreements. If the credit documentation so provides, it is possible for a creditor to appoint a director or observer to the board of the debtor. If the creditor is a bank, appointing a director could lead to risks for the bank, because bank employees are not usually entitled to perform the function of a member of the debtor's statutory body. An observer should be an independent person and the provisions on bank secrecy and business secrecy should be observed.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Debt to equity exchange in the form of debt capitalisation is possible under Slovak law if the debtor cannot repay (partially or fully) the loan to a creditor. This is usually accomplished by the lender/shareholder assigning the debt to the debtor in return for receiving shares in the debtor's company. Conditions apply to the increase in the debtor's registered capital and its articles of association for these purposes. If the shareholder is a bank, the bank's resulting shareholding in the debtor must not exceed the relevant limit on shares that a bank is entitled to acquire.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	The Slovak Act on Bankruptcy and Restructuring expressly provides for the possibility of a cram down of the restructuring plan on a dissenting minority of creditors. If the insolvency proceedings have been initiated by the debtor itself, he will also be in charge of preparing the restructuring plan. If, on the contrary, the insolvency petition was originally filed by the creditors, the restructuring plan will be prepared by the insolvency administrator. Generally, the plan must be first submitted to, and approved by, the committee of creditors. For the purpose of voting on the restructuring plan, the creditors are divided into groups according to the nature of their claims, namely secured and unsecured claims. A third group comprising the shareholders of the debtor is created if the restructuring plan will affect their proprietary rights or if the debtor is to be merged or divided. These three main groups of creditors may be further subdivided into groups according to the value of the claim, its legal grounds or economic interest. The approval is granted if a simple majority of each group votes for the plan. The restructuring plan that has been approved by the committee of creditors is then submitted to the court for approval. Where necessary, a request for substitution of dissenting creditors´ approval by court order (*Nahradenie súhlasu skupiny alebo dlžníka*) is submitted to the court together with the request for approval of the restructuring plan. The court decision on the cram down will be delivered jointly with the decision approving or rejecting the restructuring plan. However, the court may only compel the dissenting creditors to approve the plan if they will not be materially disadvantaged by the approval. The court will either approve the restructuring plan within 15 days of its submission or dismiss the plan if it does not comply with the statutory requirements, e.g. the plan is contrary to the common interest of the creditors or discriminates against one of the creditors or the process of its approval in the committee was not duly complied with. The restructuring plan approved by the court becomes binding and effective for all participants of the plan, regardless of whether they voted for it or not. As of the date of the publication of the court decision, the claims of any of creditors who did not participate in the insolvency and/or restructuring proceedings cease to exist.
7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	A company can continue to trade under court supervision while pursuing a restructuring plan, (*reštrukturalizácia*) (see question 6 above for more details) but if a bankruptcy decree is made in respect of the company (*konkurz*), it ceases its business operations and the claims of the creditors are settled pro rata from the sale of company's assets under court supervision.

DISTRESSED DEBT TRADING	
1. How does a lender sell a loan?	Non–performing loans can be transferred by a written assignment agreement. This does not necessarily require the consent of the borrower, but loan agreements usually provide for such consent. The original loan agreement stays in place and the assignment will be effective towards the debtor when it has received notification from the assignor or the assignee. If a loan is assigned, the new creditor takes over the position of the original creditor. However, it is unusual in Slovak loan agreements that an assignment of receivables is prohibited.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	Under Slovak law, security relating to receivables being assigned is automatically included in the transfer, together with all the rights attaching to the security. As a general rule, the receivables are assigned subject to the same conditions (if any) as existed prior to the assignment. It is usually advisable to define the relevant security in the assignment agreement. The assignor is obliged to deliver to the assignee any and all relevant loan and security documents and provide all information relating to the assigned receivable. The original creditor must notify the person(s) who have provided any relevant security, but there are no direct sanctions if they do not. If the receivable is secured, the security (pledge) must be registered in the Central Notarial Register of Pledges.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Slovak law does not recognise sub-participation, nor does it make a distinction between the creditor of record and a sub-participant. Arrangements of this type can be entered into on the basis of the general rules of Slovak civil law, including freedom of contract, but are not likely to have the regulatory, accounting and insolvency-related consequences usually desired by lenders.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	The purchase, sale and/or transfer of non-performing loans are not listed as banking services that require licensing by the relevant authority (the Slovak National Bank). An entity incorporated in the Slovak Republic whose business activity is sale, purchase and/or the transfer of non-performing loans can operate its business on the basis of a valid trade licence. Factoring and forfeiting are not considered as financial services, but rather as unregulated trades.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	This question needs to be examined with respect to the facts of individual cases. Theoretically, a borrower could buy certain parts of the debt that it owes to the creditor. It generally has the same effect as if the debt was repaid: the debt is extinguished. A company associated with the borrower may also buy the company's debt.

6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	A party acquiring a claim against an insolvent debtor by way of assignment after the commencement of an insolvency process would assume the position of the original creditor as its successor in the insolvency proceedings. Such an accession needs to be approved by the insolvency court. The new creditor would have the right to vote at the creditors' meeting in the insolvency proceedings.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	General provisions on bank secrecy apply to non-performing loan transfers and prevent loan data from being disclosed to a potential purchaser without the consent of the borrower. However, Slovak loan documentation typically contains a general consent by the borrower to allow the lender to disclose loan data for the purposes of selling or transferring the loan. Data protection only applies to individuals and there is an exception that applies to assignment of receivables: consent to the processing of personal data is not required where the data is processed solely for the purpose of performing the assignment agreement and/or the loan agreement. Unless the agreement provides otherwise (which is usually the case), confidential data may not be disclosed without the consent of the other contractual party.

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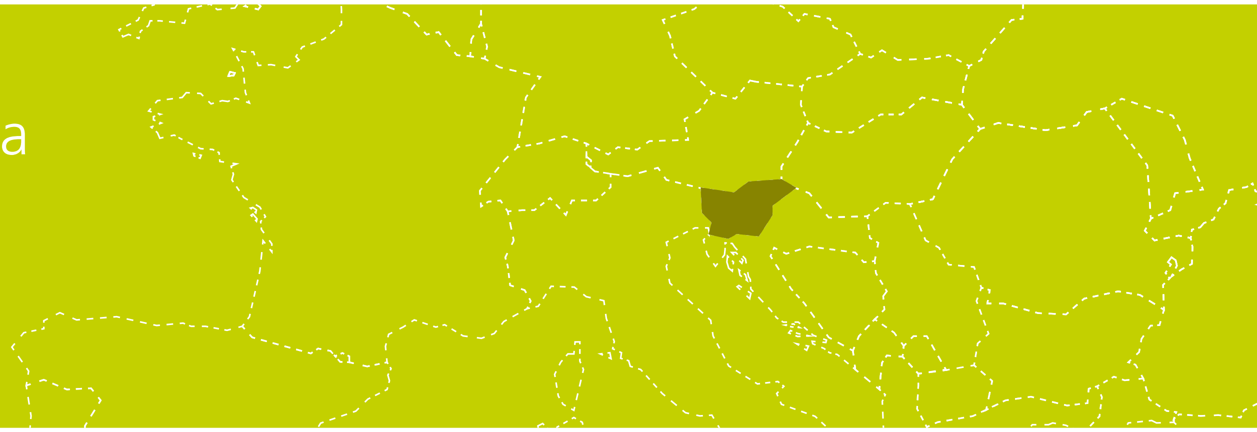

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

Under Slovenian law, when a company becomes insolvent:

(a) no payments or commitments should be made except those that are necessary for the ongoing regular operations of the company; and
(b) creditors must be treated equally.

For the purposes of Slovenian law, insolvency occurs when the debtor is unable to settle its obligations that fall due during a certain period of time. Insolvency is assumed if the debtor is more than two months late in paying one or more of its obligations that together exceed 20% of all of its obligations, shown in the annual report for the last financial year prior to the maturity of the obligations. If not proven otherwise, the debtor is also deemed insolvent if its obligations exceed the value of its assets or when its current year loss together with any loss brought forward from previous years is equal to, or greater than, half of the subscribed capital, and that loss cannot be covered by the profit brought forward or reserves. The company's management must submit a report on financial restructuring measures to the supervisory board within a month of insolvency occurring. The report must:

(i) clarify the company's financial position;
(ii) analyse the causes of insolvency; and
(iii) give the management's opinion as to whether a financial restructuring is more likely than not to succeed, and if so, provide a financial restructuring plan.

The management must apply for bankruptcy proceedings within three working days of the occurrence of any of the following:

(a) the management considers that the probability of a successful financial restructuring is lower than 50%;
(b) the general meeting does not adopt a resolution to increase capital by cash contributions when so required by the financial restructuring plan; or
(c) the contributions pursuant to the resolution to increase capital are not paid.

Members of the management board are jointly and severally liable to the company for damages arising from a breach of their obligations, unless they can prove that they have acted with the diligence of a conscientious and fair manager. Creditors of the company may also pursue a compensation claim by the company against members of the management board if the company is unable to pay their claim.

Furthermore, members of the management board are jointly and severally liable to creditors whose claims are not fully repaid in the bankruptcy proceedings if they failed to comply with their duties (e.g. they failed to prepare a financial restructuring plan or file a request for bankruptcy proceedings within the prescribed time period).

In bankruptcy proceedings, the liability of the members of the management board is limited to double the member's income during the year in which the breach occurred, subject to a minimum liability limit of EUR 150,000 for large companies, EUR 50,000 for medium sized companies and EUR 20,000 for other companies. The limit on liability does not apply if the damage arose out of deliberate acts or gross negligence.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	Under Slovenian law, granting further loans does not expose the lender to civil or criminal liability. However, if a member grants a company in financial difficulties a loan (instead of providing capital), it is not allowed to pursue the claim in any insolvency proceedings against the company as its creditor, because the loan is treated as forming part of the company's equity. This rule applies to limited liability companies and their members as well as to shareholders of joint-stock companies with more than 25% of voting shares.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	If a company in financial difficulties gives additional or extended guarantees and/or asset security, its actions may be challenged. Prior to the commencement of bankruptcy proceedings, any creditor with a due claim may challenge any act of the debtor that has caused a decrease in the funds designated for the repayment of creditors. Any disposal for value may be challenged within one year of the contested act if: (a) at the time of the disposal the debtor knew or ought to have known that the act was going to harm its creditors; and (b) the person who benefited from the performance of the act knew or ought to have known about the debtor's insolvency. If the disposal was a gift, or for no consideration, the debtor's knowledge of the harmful nature of the act is assumed, the third person's knowledge of the harmful nature of the act is not required, and the period in which the act may be contested is extended to three years. If the court grants the claim, the contested act is of no effect against the creditor, but only to the extent required to repay the creditor's claim. After the commencement of bankruptcy proceedings, any legal transaction or act, which was concluded or performed within the 12 month period prior to the application for the bankruptcy proceedings that preferred certain creditors or caused a decrease in the funds designated for the repayment of creditors may be challenged by the bankruptcy administrator or by the creditor within six months of the commencement of the bankruptcy proceedings, provided that the person who benefited from the performance of that act knew or ought to have known about the insolvency of the debtor.

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Under Slovenian law one or more of the company's creditors may be appointed as a member of the supervisory or management board provided the usual procedure for appointing a new member to these respective bodies is followed (i.e. a member of the supervisory board is appointed by a resolution of the shareholders' assembly; a member of the management body is appointed by a resolution of the supervisory board (if a company has one) or by a resolution of the shareholders' assembly). All members of the supervisory or management body are jointly and severally liable to the company for damages arising out of any breach of their duties, unless they can prove that they fulfilled their duties fairly and conscientiously. This provision also applies to any creditor representative member of the respective bodies. Creditor appointments are, therefore, not common in Slovenia because of this potential liability.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	If a debtor is a company with share capital, it may propose a debt to equity conversion. The legal requirements for converting debt to equity as part of compulsory settlement proceedings (which are a type of insolvency proceedings – see question 6 below) differ from the general provisions applicable to the increase of share capital relating to a debt to equity conversion (which qualify as an in-kind contribution) outside compulsory settlement proceedings. As one of the main principles of insolvency proceedings is the equal treatment of creditors, a debtor that is subject to insolvency proceedings must offer the same conditions of conversion to all the creditors, but more favourable conditions may be offered to holders of secured claims. If a debt to equity conversion is one of the measures proposed in the financial reorganisation plan that was submitted to the court in compulsory settlement proceedings, the general meeting of the debtor must adopt a decision to increase capital within four months of the commencement of the compulsory settlement proceedings. Within three working days of such decision, the debtor must invite the creditors to accept the offer to convert their claims into equity and thereafter submit an authenticated copy of the notarial record of the decision to the court. The increase of the share capital will only be valid if the proposed compulsory settlement (of which the debt to equity conversion is a part) is accepted. If as a result of a debt to equity conversion in relation to a publicly traded company or certain other joint stock companies, a creditor's shareholding exceeds 25% or more of the company's voting rights, the creditor is obliged to submit a takeover bid.

6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?

Under Slovenian law, there is no mechanism outside insolvency proceedings allowing the majority creditors to compel a dissenting minority to agree to a debt restructuring.

However, as an alternative to bankruptcy proceedings (which are collective terminal proceedings), the company can apply for compulsory settlement proceedings, which are intended to achieve the survival of the company. In order to commence compulsory settlement proceedings the following conditions have to be met:

- (i) the debtor company must be insolvent;
- (ii) an application for commencement of the compulsory composition proceeding must be filed by the debtor or its (personally liable) member or shareholder (legitimate applicants);
- (iii) the application must include:
  - A report on the financial standing and business of the debtor (including financial statements with explanations, a list of ordinary claims, a list of subordinated claims, a list of secured claims, and the amount of the company's average monthly operating costs (in the ordinary course of business);
  - An auditor's report, containing an unqualified auditor's opinion that the accounting report reveals a true and fair view of the debtor's financial situation and has been prepared using acceptable accounting principles;
  - A financial reorganisation plan;
  - A statement by the debtor's management that the proposed compulsory composition is more likely than not to succeed;
  - A report of a certified company value appraiser confirming that the debtor is insolvent, that the proposed reorganisation plan is feasible, and that creditors debts are more likely than not to receive a better return in the proposed compulsory composition than the alternative bankruptcy proceedings;
  - A certificate of payment of the fee for commencement of compulsory composition proceedings and of initial advance payment for pursuing a compulsory composition proceeding.

A compulsory settlement is deemed confirmed if it is accepted by a majority of all creditors whose unsecured claims represent at least 60% of the weighted value of confirmed and probably proven claims against the debtor. In this weighted calculation, a higher value is given, for example, to secured claims, than unsecured claims, and they in turn are given a higher weighted value than subordinated claims. Confirmed claims are claims that have been confirmed by the administrator and not contested by other creditors. Probably proven claims are claims that are contested either by the administrator or a creditor, and the court has decided that they are probably proven (*verjetno izkazane terjatve*). If the compulsory settlement does achieve the requisite creditor approval, it is binding on the dissenting minority creditors as well, except for those that are explicitly excluded (exclusion rights and preferential and secured claims).

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	The main purpose of compulsory settlement proceedings (see question 6 above) is to keep the debtor company as a going-concern. They cannot be used for the sale of the business as a going concern. The company's business and assets may be sold in bankruptcy proceedings. An application for the commencement of compulsory settlement proceedings is deemed to include a subordinate application for the commencement of bankruptcy proceedings. Hence, if the application for the compulsory settlement proceedings is refused or rejected, or if the compulsory settlement proceeding is terminated for any reason without being accepted, the court will then commence bankruptcy proceedings.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?	As there are no special provisions under Slovenian law that determine how the sale or the transfer of a non-performing loan should take place, the general provisions of the laws of obligation apply. It is necessary to differentiate between an assignment of a claim, which only transfers the rights of the creditor; and a transfer of a contract, which transfers all the rights and obligations of one party to another. A lender may assign a claim to a third party using an assignment agreement, unless it has been agreed otherwise or the nature of the claim prohibits assignment. Following assignment, the assignee has, in relation to the borrower, the same rights as the assignor had. The borrower's consent is not required, however the assignor must notify the borrower of the assignment. This is because prior to the borrower being notified, it may still validly fulfil its obligation to the original lender (i.e. the assignor). In the case of commercial contracts, the assignment of a monetary claim will be valid even if the originating contract provides that the assignment is not allowed. However, in these circumstances, the debtor may still validly fulfil its obligations to the original lender. As an alternative to assigning a claim, a lender may transfer a credit agreement to a third party, whereby all the lender's rights and obligations arising out of the agreement are transferred to the third party, provided that the borrower consents to the transfer.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	In an assignment of a claim, ancillary rights relating to the claim (such as a pledge, the right to interest, a contractual penalty, security and guarantees, etc) generally pass together with the assigned claim to the acquirer, without any further conditions. However, in case of those related security rights that are registered in a public register (i.e. a mortgage or pledge of book-entry securities), transfer of these related security rights will only be effective in relation to third parties if the transfer is registered in the respective register.
3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Slovenian law is silent on sub-participation agreements but does not prohibit them. They are not common in Slovenian banking practice. If an underlying credit agreement prohibits a true sale of a non-performing loan, and the lender is a bank, it can transfer some of the credit risk relating to the loan through a synthetic securitisation process. A synthetic securitisation process means a securitisation where division of the credit risk to the credit risk segments is achieved by the use of credit derivatives or guarantees, and the pool of credit risk exposures is not removed from the originator bank's balance sheet. Securitisation is regulated by the Banking Act, which mostly summarises the provisions of Directive 2006/48/EC, which in turn relates to the taking up and the pursuit of business of credit institutions. Pursuant to the Banking Act, banks may also receive additional credit insurance from debtors or third persons.

4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	In general, if the non-performing loans are purchased, sold and/or transferred by non-financial institutions, no prior authorisation or licence of any form from any regulatory authority is required. If a financial institution wishes to purchase, sell and/or transfer loans it needs an appropriate licence from the Bank of Slovenia. However, if the purchase, sale and/or transfer of a non performing loan is a one off, non-recurring transaction, no licence is required.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	The general position under Slovenian law is that any such purchase of debt is permitted and the purchase will extinguish that debt. However if a borrower purchases its own debt prior to bankruptcy, the purchase may be challenged by other creditors under general insolvency avoidance provisions (see part I question 3 above).
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	Pursuant to the Insolvency Act, a creditor gains the right to perform procedural acts in formal insolvency proceedings (e.g. to vote on the compulsory composition within the compulsory composition proceedings, or to challenge a claim registered by another creditor) if it has registered its claim in the insolvency proceedings with the court conducting the proceedings. A claim can be registered within three months of the bankruptcy proceedings being published or within one month of the compulsory settlement proceedings being published, as the case may be. A party that acquires a claim after the commencement of insolvency proceedings is entitled to execute all procedural rights (including the right to vote) in the main insolvency proceedings if: (a) the original creditor duly reported the claim in the insolvency proceedings (as described in the first paragraph above); and (b) either the original creditor or the party that subsequently acquired the claim notifies and proves the transfer of the claim to the insolvency administrator by providing him with a copy of the relevant contract.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	The Banking Act and the Personal Data Protection Act regulate confidential data protection in Slovenia, but the position in relation to the protection of a client's data involved in the sale and/or transfer of non-performing loans is not clear. However, the established practice of The Bank of Slovenia does not hinder or prevent a lender from selling and/or transferring non-performing loans.

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FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company gets into financial difficulties? Specifically: are the directors legally obliged to file for insolvency if the company is insolvent? Assuming the circumstances are such that the directors are not obliged to place the company in a formal insolvency procedure, are there steps that a board of directors should be advised to take to mitigate their personal exposure/risk?

Under Spanish law, directors are obliged to file for a declaration of insolvency within two months of the date on which they become aware (or should be aware) that the company is insolvent. Insolvency occurs when a company cannot pay its debts as they fall due.

If the directors fail to file for insolvency when required, they can incur personally liability for the company's debts. If it is the creditors that file for insolvency (instead of the directors), the effect of the procedure on the company is more severe; for example the directors' management powers are suspended and an insolvency administrator can be appointed. In addition, on a creditor filing, the company is not permitted to submit a proposal of early composition with creditors in order to restructure its debts.

Other than the obligation to file for insolvency, the directors' duties and obligations do not change when a company runs into financial difficulties. The directors remain personally liable to creditors for any damage caused to them. In order to try to mitigate their personal exposure or risk, the directors should take precautions, such as taking professional advice, holding board meetings, and avoiding agreements and decisions that could cause harm to the company's creditors although these measures are not prescribed by law.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?

Creditors can, at their own discretion, extend credit facilities to a company in financial difficulties. It is theoretically possible for a lender to incur liability for deceiving other creditors in circumstances where the extension of credit gives a false appearance of solvency, but only if there is strong evidence that the credit was extended for this purpose.

In addition, it is also possible to challenge transactions taking place in the two year period before an insolvency if they are considered harmful to the rest of the creditors. If successfully challenged, such transactions are declared null and void. However, an extension of credit that is designed to benefit both the company and creditors by providing new liquidity is unlikely to be challenged in this way.

3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?

If security is granted in connection with new credit, it is unlikely to be challenged in a subsequent insolvency unless there is any evidence of harm caused to the rest of the creditors.

However, under Spanish law, if the company grants security in respect of an existing debt, or repays a debt early (thereby improving the position of one creditor to the detriment of others) in the two year period before the declaration of insolvency, then the transaction can be challenged if it is harmful to the other creditors. If successfully challenged, the transaction would be declared null and void. In addition, if it can be shown that the creditor concerned was not acting in good faith, its credit could be subordinated and its voting rights in the insolvency procedure forfeited.

4. If a company's main lender wants to monitor the company very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	It is possible, by agreement, for a lender to appoint an observer to the company's board of directors. However if it is considered that the lender's representative has the power to influence or affect the company's management, he could be treated (and incur liability) as a de facto director. This could happen whether or not the company is insolvent.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	It is possible under Spanish law for a company to exchange some (or all) of a lender's debt for equity in the debtor. However, the corresponding capital increase would have to be approved by the existing shareholders of the company and, in principle, at least 25% of the debt (or 100% in the case of a Spanish SRL) must be due and payable. The remaining 75% of the debt must have a maturity date within five years of the capital increase. A lender wishing to exchange debt for equity that is not already a shareholder of the debtor should be aware that under Spanish law, the debt of shareholders who hold 10% or more of the debtor's stock capital (or 5% in the case of a listed company) is subordinated to the debt of other creditors.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are open to the company/the majority creditors to compel the minority of dissenting creditors to agree?	There is a new out-of-court restructuring procedure, introduced in 2009, that allows a refinancing to be put in place with the consent of holders of at least 60% of the company's total debt. The refinancing agreement must satisfy certain criteria, including increasing or extending the facilities available to the debtor within the framework of a viability plan, and in order to be beyond the scope of subsequent avoidance actions, the agreement and viability plan must be confirmed by an independent expert and issued as a public deed. Provided the agreement is observed by the debtor, it remains binding on all creditors and enables the debtor to avoid insolvency proceedings. If the debtor fails to observe the terms of the agreement, it must file for insolvency. Since its introduction, this procedure has been popular. A company that is in insolvency proceedings can restructure its debts if a majority of creditors holding at least 50% of its ordinary debt agree (subject to a number of exceptions). The restructuring becomes binding on the dissenting minority. In addition, a report regarding, among others, the viability plan and the proportionality of the guarantees with respect to the normal market conditions must be issued by an independent expert appointed by the Commercial Registry. Subsequent to this legal amendment, most of the refinancing transactions have been formalized complying with those requirements.
7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business for as much money as possible?	Under Spanish law there is only one statutory insolvency procedure available (*concurso*). The aim of the procedure is to find a means of rescuing the company either by supervising its management, or by substituting the directors and trying to reach a restructuring agreement with its creditors (see the answer to Q6 above). While this process continues, the company continues to trade in the ordinary course of business until the eventual liquidation phase. If a rescue or restructuring is not possible, the procedure continues as an orderly liquidation of the company's assets and distribution to creditors.

DISTRESSED DEBT TRADING	
1. What are the basic requirements of a "true sale" of a non-performing loan (e.g. how does a lender transfer a non-performing loan)?	A non-performing loan can be transferred by an assignment, which must be executed as a public document to ensure that it is effective against third parties. Where the loan has been fully drawn (so that only credit rights are being assigned), the borrower's consent is not required, unless the loan agreement provides otherwise. If the loan is not fully drawn, the borrower's consent to the assignment is needed. In either case, the borrower must be notified of the assignment to avoid his obtaining discharge by payment to the assignor.
2. Are the various forms of security in relation to the non-performing loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the non-performing loans.	All ancillary rights (including any security, guarantee, privilege etc) attached to the assigned debt are transferred automatically to the assignee. However, some formalities may be required to complete the transfer in respect of certain ancillary rights, for example: recording the transfer of mortgages, chattel mortgages and pledges without displacement of possession in public registries, giving notice to the corresponding debtors regarding pledges over receivables etc.
3. If the underlying credit agreement prohibits a "true sale" (i.e. a change in the lender of record) how else (if at all) can a lender off-load some of the risk/ benefit in the loan? E.g. does your jurisdiction permit sub-participations agreements?	It is unusual under Spanish law for loan agreements to prohibit the assignment of the loan by the creditor, but sub-participation agreements are permitted in any event. In a sub-participation arrangement, the ancillary rights and securities are not assigned to the sub-participant, who is not effectively protected in the event of enforcement, or insolvency of the borrower because the sub-participation agreement only creates a personal obligation between the lender and sub-participant. It does not create any direct rights in favour of the sub-participant against the borrower.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	No licence or authorisation from a regulatory authority is required because the purchase of credit or loans, even if carried on as a business, is not a regulated activity in Spain. Under Spanish law, the only regulated activity that requires a credit licence is taking refundable deposits from the public in the form of deposits, loans, temporary transfers of financial assets etc.
5. Is a borrower or a company associated with the borrower permitted, as a matter of law (i.e. assuming that the credit agreement does no expressly prohibit it), to buy certain of the debt that it owes to a lender/ lenders?	Yes, either the borrower, or a company associated with the borrower, could acquire the borrower's debt. Upon acquisition by the borrower itself, the debt would be extinguished. If a company associated with the borrower acquires the debt and the borrower subsequently becomes insolvent, the associate company creditor is regarded as a special related party and the debt would be subordinated by law.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the acquirer of the claim/debt have the right still to vote that claim in the insolvency process?	Under Spanish law, a purchaser who acquires debt after the declaration of insolvency has no right to vote in relation to the acquired debt in the framework of the insolvency process.

7. Are there any issues regarding data protection and bank secrecy laws in your jurisdiction which would hinder or prevent a lender from selling and/or transferring non-performing loans?

No. However, before the loan assignment occurs, no personal data can be assigned or disclosed even to the potential purchaser unless such information is properly dissociated by separating the financial information from personal data. Once the loan transfer has taken place, the assignment of the corresponding personal data is expressly allowed under Spanish law, because it is considered necessary to enable the assignee to manage the assigned loans.

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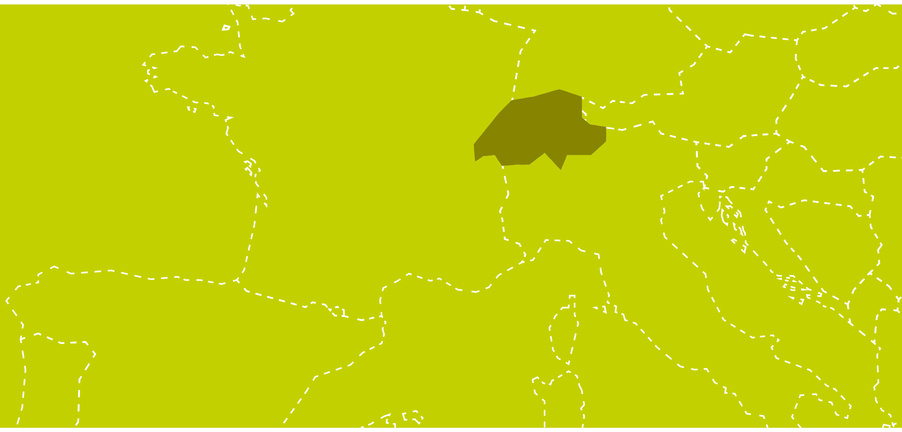

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company runs into financial difficulties? Specifically: are directors legally obliged to file for insolvency if the company is insolvent and, if not, what steps should a director take to mitigate any risk to him/her personally?

In Switzerland, members of the board of directors and the managing board of a company (*formelle Organe:* formally appointed directors and officers) and any persons engaged in the management of the company (*faktische Organe:* de facto or shadow directors) owe a general duty of care and loyalty to the company, and are subject to a corresponding liability for intentional or negligent breach of this duty.

Directors and officers are required to act in the best interests of the company. In the event of a conflict between the interests of the various stakeholders, the directors and officers must exclusively safeguard the interests of the company.

If a company gets into financial difficulties, the following additional duties apply that are intended to safeguard the interests of the creditors as well as the company.

If the most recent annual financial statements show that the company has suffered a loss exceeding the value of half its share capital, the directors and officers are under a duty to convene a shareholders' general meeting to propose restructuring measures designed to avoid insolvency and to ensure the company's survival as a going concern. The duty to convene a shareholders' (restructuring) meeting in these circumstances is a director's core duty that cannot be delegated. In case the board (unjustifiably) fails to convene the meeting, the auditors have to inform the board and the shareholders and, ultimately, the auditors have to convene a shareholders' meeting.

Under Swiss law, a company is over-indebted if it is balance sheet insolvent, which occurs when its liabilities exceed its assets, both on a going-concern and on a liquidation value basis. If a company becomes over-indebted, unless creditors subordinate their claims sufficiently to rectify the balance sheet problem, the board of directors must notify the insolvency court. Unlike in other jurisdictions, the duty of the directors to notify the bankruptcy court (*Konkursantragspflicht*) is only triggered if the company is over-indebted. The duty does not apply in the event of the company's illiquidity (or where it ceases payments). However, despite necessitating a notification to the bankruptcy court, over-indebtedness does not automatically trigger a duty to file for insolvency if there are reasonable and concrete prospects for a restructuring of the company that are expected to cure the over-indebtedness within a reasonably short period of time.

During any period when the company is over-indebted, the directors and officers must treat all unsecured creditors (including suppliers, customers and employees) equally, and may not prefer any creditors over other creditors or enter into transactions adverse to the company. Otherwise, directors may incur liability for intentional or negligent breach of the duty of care and loyalty to the company. Furthermore, such transactions could be subject to avoidance actions (see the answer to the question below).

	Finally, the directors are under a duty to initiate winding up procedures or restructuring procedures if required to do so by: (i) the company's articles of incorporation; (ii) a resolution of the general meeting of shareholders; (iii) organisational insufficiencies; or (iv) if the company's business purpose is immoral or illegal. If the company enters bankruptcy proceedings, the board members may become personally liable jointly and severally with the company for unpaid withholding taxes and VAT unless they can prove that they took all reasonable measures in order to determine and comply with the tax demand. Further, if certain conditions are met, directors may become liable for unpaid social security contributions.
2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	A lender that extends credit facilities to an insolvent company can incur liability to other creditors of the company if it can be shown that the extended facilities delayed the onset of bankruptcy, and caused the company's indebtedness to increase. In addition, any repayments made or security granted in respect of any such extended loans can subsequently be avoided by other creditors or the administrator if the payments were effected in order to prefer certain creditors, to disadvantage certain creditors or if the security was granted to secure existing, and to date, unsecured obligations, provided the debtor was insolvent at that time and the repayment or the granting of security occurred during a period of time of one or five years, respectively, prior to the opening of bankruptcy proceedings. Secured loans granted by third parties within the framework of a formal restructuring are exempt from these avoidance provisions. In bankruptcy proceedings, shareholder loans can, in exceptional cases, be treated as subordinated if the loans were granted to an insolvent company for restructuring purposes (i.e. not for a specific business project).
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	As discussed in question 2 above, the granting of security in such situations may be subject to challenge by other creditors and/or the administrator if the company subsequently enters into bankruptcy proceedings. Therefore, before entering into any such transaction the parties need to consider carefully any up, down, or cross-stream issues, as well as the structuring of the credit facility within the framework of the formal restructuring. Additionally, the directors and/or officers of the company granting such security may be subject to criminal liability. If the company is declared bankrupt, or if a loss certificate is issued against the company, the directors can be prosecuted for: (i) harming creditors by diminishing assets, (ii) mismanagement (i.e. causing or aggravating over-indebtedness, causing insolvency or aggravating the financial situation) or (iii) preferring creditors (i.e. paying undue debts, paying with unusual means of payment or causing the company to voluntarily grant security for existing debts). Such behaviour can result in up to five years imprisonment or a fine.

4. If a lender wants to monitor its borrower very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	If the lender is also a shareholder, it can have one of its officers appointed as a director. The appointed individual would become subject to the same duties and liabilities as the other directors. Alternatively, lenders can agree contractual provisions entitling them to appoint an observer to the board of directors. Depending on the power granted to, or claimed by, such observer and the decisions taken and the influence exerted by him, this person (and, indirectly, the creditor) may become a de facto director and, as a consequence, be subject to the same duties and liabilities as a formally appointed director. For this reason, professional lenders in Switzerland tend to be reluctant to appoint observers to the borrower's board. Instead, they generally seek to limit their influence on the borrower's business decisions.
5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Swiss law allows creditors to convert debt into equity provided certain conditions are satisfied. In particular, the board of directors must confirm the existence of the creditors' claims that are being exchanged, and the auditors have to review the board of directors' report on the capital increase. Additional requirements apply if the debt was established at the outset with the intention of converting it into equity. If the requirements are not met, the commercial registry can refuse to register the capital increase.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are there to compel the minority of dissenting creditors to agree?	Under Swiss law, a composition by order of the court can be used as a compulsory settlement process in order to avoid the company's liquidation. The procedure can be used either before or during bankruptcy proceedings, and in the case of bankruptcy proceedings, the bankruptcy decree may be revoked by means of a composition. A composition by order of the court is based on a proposal by the debtor (in the form of an ordinary composition agreement or composition agreement with assignment), which must be approved by a qualified majority of creditors consisting of either: the majority of creditors representing two thirds in value of the overall claims; or one quarter of the creditors representing three quarters in value of the overall claims. In calculating these majorities, preferential creditors are not counted and secured creditors are counted only to the extent of their estimated shortfall. Finally the composition agreement has to be confirmed by the composition court, following which it becomes valid and binding upon all creditors. Unlike in bankruptcy, a composition agreement does not generally restrict a secured creditor's right to enforce its security, either by way of official enforcement proceedings or (if agreed upon) by way of a private enforcement. However, a composition agreement can provide for a stay on the enforcement of security for a certain period of time during liquidation (one to two years has been held to be admissible). Two important consequences of a composition are that: no interest has to be paid on unsecured debt (unless the composition agreement provides otherwise) and an administrator is appointed to supervise the business decisions of the officers and directors. A composition by order of the court must be distinguished from an out-of-court composition, which is purely contractual, and therefore consensual. A separate composition is agreed with each individual creditor and it requires the consent of all parties to become binding.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business?	While bankruptcy proceedings are geared towards liquidation, ordinary composition proceedings (i.e. composition agreements other than composition agreements with an assignment of assets) are geared towards debt rescheduling and reorganisation. Ordinary composition proceedings typically allow a company both to continue its business operations (under the supervision and instructions of an administrator) and to try to agree a deal with its creditors for a period of four to six months (and in exceptional cases up to 24 months). However, during this period, the capacity of the company to divest, encumber or pledge assets, to give guarantees or to make gifts is limited by the corresponding authorisation of the composition court. If the company contravenes those restrictions or the administrator's instructions, and the administrator reports this to the composition court, the latter may revoke the debtor's capacity to dispose of its assets or cancel the moratorium. During the moratorium period, enforcement proceedings cannot be initiated or continued except for enforcement proceedings in relation to certain specified priority claims (including some employee and pension related claims) and enforcement proceedings for the realisation of collateral for claims secured by a mortgage of real estate. Limitation and peremptory deadlines cease to run, and interest stops accruing against the company, in respect of unsecured claims. Real estate may not under any circumstances be realised. If the company is not successful in concluding a deal within the time period granted, creditors can apply to the court for the opening of bankruptcy proceedings. The composition agreement with assignment of assets can empower the creditors to sell or otherwise dispose of the company's assets, or the assets can be assigned in whole or part to a third party. In both cases, i.e. whether the assigned assets are realised by way of liquidation or assigned to a third party, the proceeds realised are used to satisfy the claims of the creditors.

DISTRESSED DEBT TRADING

1. How does a lender sell a loan?	Under Swiss law transferring title in receivables requires: (i) an agreement creating the obligation to pass title (such as a sale and purchase of receivables or a security agreement creating security rights in the receivables); (ii) the transferor to have title to the receivables and be able to freely dispose of them; and (iii) a written assignment constituting the act of disposal. If all three requirements are satisfied, title will pass irrespective of whether the receivables are being transferred outright or only for security purposes. Unlike other jurisdictions, under Swiss law, no notification of the third party debtor is required for an assignment of receivables to be effective. However, as long as the debtor has not been notified of the assignment, it may obtain discharge by paying the assignor.
2. Are the various forms of security in relation to the loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the loans.	An assignment of receivables automatically includes corresponding preferential rights and certain ancillary rights such as collateral security, provided the security is of an accessory nature (such as a pledge or a suretyship (*Bürgschaft*), but not a guarantee). All other types of security must be created afresh following the assignment.

3. If the underlying credit agreement prohibits novation (i.e. a change in the lender of record) how else (if at all) can a lender transfer the economic risk and/or benefit in the loan? For instance, are sub-participation agreements allowed under the law of your jurisdiction?	Sub-participation is permitted under Swiss Law, however, only the original creditor is entitled to enforce any rights against the debtor; the sub-participants are not allowed to do so and have no corresponding claims against the debtor.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	The mere sale and purchase of loans does not require any licence or authorisation, but financing the transaction can give rise to banking licence issues. Additional banking licence issues may arise where the acquirer intends to grant additional facilities to the debtor after purchasing the distressed debt. There may also be tax implications, in particular regarding the so-called "10/20 non-banks rule" (especially where there are syndicated loans). Adverse tax consequences may be triggered if a debtor has more than ten non-bank creditors lending money on identical terms, or more than 20 non-bank creditors lending money on different terms, or where real property serves as collateral security with respect to foreign creditors.
5. Is a borrower, or a company associated with the borrower, permitted as a matter of law (assuming that the credit agreement does not prevent it) to buy debt that it owes to its lenders?	With the creditor's consent, a borrower is permitted by law to buy its own debt. Care must be taken to ensure that the purchase of debt in this way does not constitute an undue preference of one or more creditors at the expense of other creditors. Alternatively, but also subject to the rules on avoidance, an associated company might agree with the borrower to pay some or all the borrower's debts (without the creditors knowing that the associated company has paid instead of the borrower). However, this would only be allowed to the extent the associated company does not become insolvent as a result of the payments and that it was in the interests of the associated company to do so (see the answer to the answer to Part I Question 1 above).
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the purchaser of the claim/debt have the right to vote that claim in the insolvency process?	It is possible to purchase a claim against an insolvent debtor from an existing creditor at any time until the conclusion of the insolvency process. However, that purchaser must bear any costs incurred by the administrator as a consequence (for example, in connection with notices that must be re-sent, or plans that have to be adapted, etc.). The new creditor acquires the outgoing creditor's right to vote in relation to the claim in the insolvency process.
7. Are there any data protection or confidentiality issues in your jurisdiction which would hinder or prevent a lender from selling and/or transferring loans?	Data protection laws may prove an obstacle where it is intended to transfer the non-performing loan abroad, if the debtor has not previously given its consent for such a data transfer. If the transferring lender is a bank, then banking secrecy matters are relevant. However, banks typically provide for a general waiver in their documentation to get around this problem.

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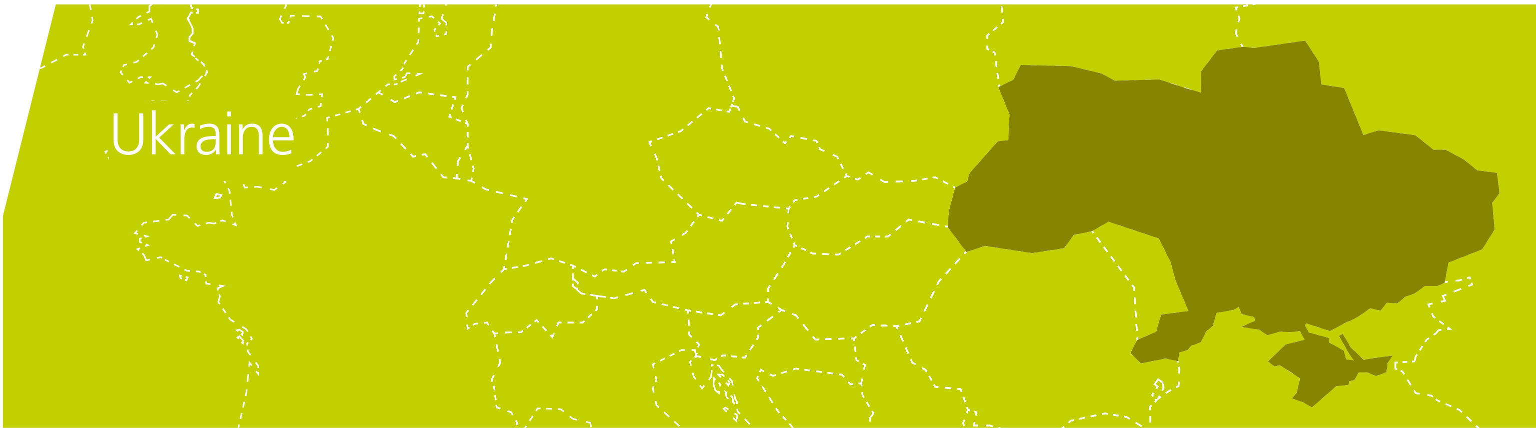

FINANCIAL RESTRUCTURING ISSUES

1. Broadly speaking, how are a director's duties and obligations affected when a company gets into financial difficulties? Specifically: are the directors legally obliged to file for insolvency if the company is insolvent? Assuming the circumstances are such that the directors are not obliged to place the company in a formal insolvency procedure, are there steps that a board of directors should be advised to take to mitigate their personal exposure/risk?

Under Ukrainian law, a governing body or a representative, who acts on behalf of a company pursuant to its constitutional documents or pursuant to the general law, must act in the company's interests, in good faith and reasonably, and must not exceed his authority. Accordingly if a company gets into financial difficulties, the directors are expected to take measures such as seeking professional advice, holding regular board meetings, informing the shareholders about the company's status and potential future risks, etc, but these measures are not prescribed in law.

If, after the end of the company's second and each following financial year, the net assets of either a joint stock company (*"JSC"*) or a limited liability company (*"LLC"*) drop below the stated charter capital of such company, the charter capital must be reduced accordingly. If net assets of either a JSC or an LLC drop below the statutory minimum charter capital for such type of company, then the company automatically becomes subject to liquidation. Ukrainian law does not expressly state who is responsible for the monitoring and enforcement of the net assets rule and what the enforcement mechanism should be.

If a company is insolvent (i.e. its assets are worth less than its liabilities), the directors must convene an extraordinary general meeting of shareholders if it is a JSC, or a general meeting of participants if it is an LLC.

A debtor must file for bankruptcy proceedings within one month of the date on which one of the following events occurs:

- (a) paying the demands of one or more creditors would result in the debtor's inability to meet its obligations to other creditors in full;
- (b) the management of the debtor decides that the debtor must file for bankruptcy proceedings; or
- (c) in the course of the debtor's liquidation (other than that related to the bankruptcy procedure), the debtor is unable to pay its creditors in full.

Failure to file for bankruptcy in the circumstances described above can give rise to criminal liability for concealment of continuous insolvency of the company. Moreover a director and/or the head of the liquidation committee of the debtor company can be held jointly liable for the debtor's unpaid creditors' claims for failure to file for bankruptcy proceedings in the circumstances described in (c) above.

2. Can creditors indefinitely extend credit facilities to a company in financial difficulties?	Ukrainian law does not expressly prevent a Ukrainian or foreign lender from granting further loans to a borrower in financial difficulties, or agreeing to reclassify debt as equity. However, at each of the two consecutive stages of the debtor's bankruptcy proceedings, (financial rehabilitation and liquidation), the validity of an agreement documenting a further loan to a borrower entered into within certain periods before the bankruptcy may be challenged by, respectively, a court-appointed financial rehabilitation manager or a liquidator of the debtor. Specific voidable transaction provisions also apply to insolvent banks that are subject to a temporary administration procedure. The directors should exercise any right to receive extended loans with caution, as they may be subject to criminal liability if the extended loans are later found to have helped cause the debtor's bankruptcy. Creditors can, within the context of actions aimed at preventing the bankruptcy of the debtor, provide financial aid to the debtor in an amount sufficient to meet the creditors' claims and to restore its solvency. Under Ukrainian legislation, financial aid can be refundable or non-refundable. In the case of refundable financial aid, it is not possible to claim interest or any other type of compensation as payment for the use or cost of funds. Finally, there is no prohibition on extending loans to a company that is already subject to bankruptcy proceedings. At the initial stage of the bankruptcy proceedings (i.e. property administration), any entry into a loan agreement by a director or the management body of the debtor is subject to approval by the court-appointed property administrator (bankruptcy trustee). At the subsequent rehabilitation stage, when directors and other management bodies of the debtor are replaced with a financial rehabilitation manager elected by the creditors and approved by the court, that manager has the authority to enter into loan agreements on behalf of the debtor. If the value of the loan agreement exceeds 1% of the book value of the debtor's assets, the transaction must be authorised by the creditors' committee.
3. If a company is in financial difficulties and the group's principal financial creditors are offering support conditional on additional or extended guarantees and/or asset security being given, what issues does this give rise to, for both the company and the (secured) creditor?	Ukrainian law does not expressly prevent a lender from providing a company in financial difficulties with financial support that is conditional on additional or extended guarantees or security over assets being given. However, such a lender will need to be concerned with provisions enabling a subsequent financial rehabilitation manager or liquidator to challenge or refuse to perform certain pre-bankruptcy transactions on grounds such as the agreement was a related party loss-making transaction, or that it offends the pari passu principle.
4. If a company's main lender wants to monitor the company very closely (i.e. more closely than the usual information covenants in the credit agreement permit), what options are there?	Under Ukrainian law, a lender does not have any statutory right to appoint a director of the company. Contractually, the lender may be granted certain rights in this respect, provided that the shareholders of the company give their consent. There is no alternative way in which a lender's nominee can be appointed as an observer or director to the board of directors of the company. If the company enters bankruptcy proceedings, the lender can participate in the nomination by creditors of a property administrator, and it can seek appointment to the creditors' committee by creditors' vote.

5. Is it possible for a lender and company to agree to exchange certain (or all) of the lender's debt for equity in the company? What issues does this give rise to, for lender and company and what consents are required?	Debt for equity conversion is not possible for LLCs because of a rule of law that provides that a participant in an LLC cannot be released from its obligation to make a contribution to the charter capital of a company. In other words, a participant in an LLC cannot discharge its obligation to make a capital contribution to the LLC by setting off its claim to an outstanding debt owed to it by the LLC against its unpaid portion of the capital contribution. It is not clear whether or not the prohibition extends to bankruptcy proceedings. The position of JSCs is different. Prior to bankruptcy proceedings, a JSC can enter into a debt to equity conversion agreement. Shareholder consent is required for the increase in charter capital. Special arrangements apply to banks that are subject to a temporary administration procedure. As part of bankruptcy proceedings, a JSC can enter into a debt to equity conversion pursuant to either a financial rehabilitation plan or an amicable settlement agreement. As part of one of these arrangements, the equity exchange can either involve newly issued shares, or sometimes existing shares that belong to existing shareholders. Usually (but not always) the consent of the owners of the existing corporate rights is required. Finally, debt to equity conversions may need prior approval of either the Anti-Monopoly Committee of Ukraine, or, in the case of a debtor bank, the National Bank of Ukraine, if the creditor/shareholder's resulting voting rights after the exchange exceed certain percentage thresholds. The approval process for these bodies is approximately 45 and 30 days respectively.
6. If the majority in value of a company's creditors have agreed the terms of some kind of debt restructuring with the company, what mechanisms/tools (if any) are open to the company/the majority creditors to compel the minority of dissenting creditors to agree?	Prior to the commencement of bankruptcy proceedings, Ukrainian legislation does not provide a mechanism to compel a minority of dissenting creditors to agree to a debt restructuring. Any pre-bankruptcy debt restructuring must therefore be entirely consensual. After bankruptcy proceedings have commenced, there are two mechanisms available to compel a minority of dissenting creditors to agree to a debt restructuring. The first mechanism is a financial rehabilitation plan, which must be formulated within 3 months of the start of the financial rehabilitation proceedings by the financial rehabilitation manager, and submitted to the creditors' committee for approval. The financial rehabilitation plan is approved at the meeting of the creditors' committee if the plan is supported by more than 50% of the committee member's votes. Lastly, the plan must be sanctioned by the court, following which the debtor's activity is reorganised accordingly and the claims and rights of the creditors and the other parties concerned are modified as provided for in the plan. The second mechanism is an amicable settlement agreement, which is available to the debtor at any stage of bankruptcy proceedings (i.e. property administration, financial rehabilitation or liquidation). Under an amicable settlement agreement, the debtor and creditors agree that certain categories of creditors' claims are either deferred, paid by instalments, or written off from the debtor's balance sheet. A decision to enter into an amicable settlement agreement is taken by a majority vote of the creditors' committee on behalf of the creditors. The agreement also requires the consent in writing of all secured creditors and sanction by the court, following which, the debtor's liabilities are restructured and modified as provided for in the agreement. An amicable settlement agreement cannot impose worse conditions for the minority of dissenting creditors (or for the creditors who did not participate in the voting) as compared with the assenting creditors of the same class.

7. Of the formal statutory procedures available to a company that is in financial difficulties, which one (if any) enables the company to continue to trade and continue to explore either: (a) a consensual deal with creditors that will see the company itself survive; or (b) an orderly sale of the company's assets/business for as much money as possible?	Financial rehabilitation proceedings (which are a form of bankruptcy proceedings) enable a company to continue to trade and explore either a consensual deal with creditors that will see the company itself survive, or, if a consensual deal cannot be achieved, an orderly sale of the company's assets or business. For more detail on the financial rehabilitation plan procedure please see the answer to question 6 above.

DISTRESSED DEBT TRADING

1. What are the basic requirements of a "true sale" of a non-performing loan (e.g. how does a lender transfer a non-performing loan)?	Contractual rights or monetary obligations under a non-performing loan (the "receivables") can be assigned. If an assignment of receivables is for monetary consideration, it takes the form of a sale and purchase of receivables. The assignment is a written agreement between the assignor and the assignee, which must otherwise follow any formal requirements (i.e. notarisation, registration, etc) of the loan agreement that is being assigned. The assignability of receivables is determined under the law that governs the loan agreement that is being assigned.
2. Are the various forms of security in relation to the non-performing loans automatically included in the transfer? If not, please describe how a lender can transfer various forms of security in relation to the non-performing loans.	In a change from earlier legislation, an assignment of receivables no longer automatically includes any corresponding security rights. Accordingly, it is recommended that the assignment agreement contain an express provision for the simultaneous transfer to the assignee of any such security rights. If any such security rights need to be registered (for example a mortgage), then, upon the assignment or other transfer to a new beneficiary, such security interest must be re-registered in the name of the new beneficiary.
3. If the underlying credit agreement prohibits a "true sale" (i.e. a change in the lender of record) how else (if at all) can a lender off-load some of the risk/ benefit in the loan? E.g. does your jurisdiction permit sub-participations agreements?	Since Ukrainian legislation is silent with respect to sub-participation agreements, it can be presumed that a sub-participation agreement will be valid under Ukrainian law, provided it complies with the general principles of the Ukrainian civil legislation; however, they are not common.
4. Regulatory issues: is any form of licence or prior authorisation from any regulatory authority required for the purchase, sale and/or transfer of loans? Does it fall within the definition of providing banking or financial services in the territory of the assignor or the borrower?	The mere execution or entry into an agreement for the purchase, sale, or transfer of a non-performing loan does not require any authorisation or licence from the Ukrainian regulatory authorities. However, performance of such an agreement (i.e. repayment of the loan by the borrower to the assignee creditor) may, in some cases, require authorisation from the National Bank of Ukraine in a form of a supplement to the cross-border loan registration certificate, or an individual license for payments abroad or foreign currency settlements on the territory of Ukraine.

5. Is a borrower or a company associated with the borrower permitted, as a matter of law (i.e. assuming that the credit agreement does no expressly prohibit it), to buy certain of the debt that it owes to a lender/ lenders?	There is no specific provision in Ukrainian law that prohibits a borrower or a company associated with the borrower from buying a portion of its own debt. However, if the borrower buys all the debt it owes to a lender, the obligation between the borrower and that lender will terminate, as the borrower effectively repays and/or settles the debt with the lender as a result of the transaction.
6. If a party acquires a claim against an insolvent debtor after the commencement of an insolvency process, does the acquirer of the claim/debt have the right still to vote that claim in the insolvency process?	Ukrainian legislation is not clear in this respect. On a conservative interpretation, the acquirer of the claim would have a right to vote in relation to that claim in the bankruptcy proceedings only if the assigned claims are acknowledged by the debtor or a Ukrainian court and are included by the property administrator in the debtor's register of creditors' claims. A participation petition substantiating the creditor's claims against the debtor must be filed within 30 days from the formal publication in a Ukrainian governmental newspaper of a notice regarding commencement of the bankruptcy proceedings against the debtor. Claims not presented by the specified deadline are deemed to be discharged or extinguished.
7. Are there any issues regarding data protection and bank secrecy laws in your jurisdiction which would hinder or prevent a lender from selling and/or transferring non-performing loans?	Where the lender is a commercial bank, it is required by law to preserve the confidentiality of any information concerning its clients, including any information regarding the existence or the terms of any loan agreement. In addition, the loan agreement itself may contain provisions restricting the disclosure by the bank to a third party (other than an authorised state body) of information regarding the agreement. In each case such information may be disclosed to the prospective buyer only with the express prior written consent of the client. Similar to the banking legislation, the legislation governing the collection, storage and use of information and the protection of consumer rights contains a general prohibition on unauthorised disclosure to a third party (other than to competent state authority and only to the extent prescribed by law) of any information regarding an individual collected by any entity in the course of its activity. Save for this general prohibition, such legislation does not specifically address any issues related to transfers of non-performing loans.

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