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Spanish restructuring plans in a nutshell

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Directive (EU) 2019/1023 of the European Parliament and of the Council of 20 June 2019 on preventive restructuring frameworks, on discharge of debt and disqualifications, and on measures to increase the efficiency of procedures concerning restructuring, insolvency and discharge of debt, and amending Directive (EU) 2017/1132 ("**EU Restructuring Directive**") entered into force on 16 July 2019. The EU Restructuring Directive has been transposed into Spanish law through the bill to reform the Insolvency Law, which was approved on 25 August 2022 by the Spanish Parliament and will come into force 20 days after its publication in the Official State Gazette (BOE).

Following the principles of the EU Restructuring Directive, the new Spanish restructuring framework increases flexibility and provides alternative methods to successfully restructure viable businesses, and navigate and overcome insolvency crises.

This bullet-point summary provides an overview of key aspects of the new Spanish preventive restructuring framework based on the approved legislation amending the Spanish Insolvency Law.

GENERAL OVERVIEW

- Cram-down restructuring process to be negotiated out-of-court and with minimum court involvement (and without entering into formal insolvency proceedings).
- Available in the event of:
  - **Actual insolvency** → cash-flow test.
  - **Imminent insolvency** → actual insolvency expected within the next three months.
  - **Likelihood of insolvency** → actual insolvency objectively expected within the next two years.
- Stay of individual enforcement actions to avoid opportunistic actions from creditors is available.
- Public or confidential options.
- Debtor-in-possession.
- Restructuring expert (if appointed by the court) or creditors representing >50% of the affected debt may apply to suspend a voluntary insolvency petition filed by the debtor, provided that negotiations are ongoing without a stay request and that a restructuring plan is filed with the application to suspend.
- New treatment of interim financing and new money, provided that the restructuring plan is judicially approved (*homologado*) and it affects specific debtors' liability majorities: protection against claw-back, equitable subordination and 50% of interim financing and

new money considered as a post-insolvency claim (*crédito contra la masa*) if insolvency ensues.

- Cross-border application: public restructuring plans and stays automatically recognised under Regulation (EU) 2015/848 of the European Parliament and of the Council of 20 May 2015 on Insolvency proceedings (Recast) (the "**European Insolvency Regulation**").

EXTENSION OF THE STAY

- Debtor may inform the court that it has commenced negotiations with its creditors with a view to reaching a restructuring plan.
- Three-month term to negotiate with creditors:
  - Extendable up to an additional three months at the request of the debtor or creditors representing >50% of the potentially affected debt, and subject to a status review of the negotiations by the judge.
  - Extension may be lifted by the judge in specific situations.
- Duties to file for insolvency or to dissolve due to impaired capital are suspended while the stay remains in place.
- Protection against involuntary insolvency petitions filed by creditors.
- The stay of enforcement action affects:
  - assets/rights necessary to operate the business (and actions to enforce any associated security);
  - non-necessary assets, or specific creditors or classes of creditors if requested by the debtor and the court decides that such a stay is needed to protect negotiations; and
  - third-party security interests and guarantees granted by group members who are not party to the stay petition, in order to avoid both the debtor and the guarantor becoming insolvent.
- The stay does not apply to public creditors or creditors who by law cannot be affected by the restructuring plan.
- *Ipso facto* clauses or other provisions suspending, modifying or terminating contracts with outstanding reciprocal obligations as a consequence of the stay are unenforceable.
- Existing contracts can be suspended, modified or terminated on general grounds.
  - Exception: during the stay, contracts necessary to operate the business cannot be suspended, modified or terminated based on breaches that occurred prior to the stay.
  - Court to decide if contracts are necessary to operate the business.

- In no event can supply agreements for assets, services or energy be suspended, modified or terminated unless agreements have been agreed on an organised market place (OMP).

FLEXIBILITY AND SCOPE OF RESTRUCTURING PLANS

- Significant flexibility. The restructuring plan can establish hair-cuts, extensions, debt-for-equity swaps, debt-for-asset deals, sales of assets, third-party releases, effects on reimbursement claims of guarantors, etc.
  - With respect to financial claims guaranteed by the Spanish Credit Institute (ICO), the restructuring plan cannot establish debt-for-equity swaps, changes to the debtor or to the governing law, or the conversion of such financial claims into a PPL or another debt instrument.
  - Banks which are beneficiaries of that ICO guarantee would need prior authorisation from the tax authorities to vote in favour of a restructuring plan that provides measures other than those referred to in the above paragraph. Without such authorisation banks would lose the guarantee.
- The restructuring plan can provide for the sale of part or all of the business as a "going concern".
- The scope of the debt affected by the restructuring plan can be limited (but must represent at least 51% of the total liabilities and the restructuring plan must be judicially approved to ensure claw-back protection).
- The plan can cram-up shareholders and cram-down nearly all types of claims (including contingent ones), except for employment, tort, family-maintenance, and future claims under existing contracts.
- If the restructuring plan involves a merger, demerger or hive-down, creditors may challenge the plan but do not have a right to oppose it under corporate law.
- If the plan provided for a capital reduction to zero to compensate losses and a simultaneous capital increase, shareholders would not have a pre-emptive right to subscribe new shares.
- The effects of the plan on public claims are very limited.
- Effects on existing agreements with outstanding mutual obligations:
- *Ipso facto* clauses or other contractual provisions suspending, modifying or terminating contracts as a consequence of the plan are unenforceable.
  - Change-of-control clauses are unenforceable in the event of a change of control over the borrower as a consequence of the plan.
  - Existing agreements may be terminated unilaterally to facilitate restructuring and avoid insolvency. Damages claims would fall within the plan.

- The plan may also suspend or terminate agreements with senior executives. The judge may limit golden parachutes to the maximum permitted redundancy settlement under employment law.

- Both borrowers and affected creditors are entitled to file for judicial approval of a restructuring plan.

CLASSES OF CREDITORS – AN ESSENTIAL ASPECT OF THE PLAN

- Creditors are grouped into classes and vote within their assigned class.
- Flexible criteria for class formation:
  - General principle: creditors within the same class should share a "common interest", according to objective criteria.
  - Claims with the same insolvency ranking are deemed to share a common interest.
  - Sub-classes can be created on justifiable grounds (financial/non-financial claims, potential conflicts of interest between creditors of different classes, etc.).
  - Secured claims form a separate class. Sub-classes within classes of secured creditors may be formed according to differences in collateral.
  - When affected by the restructuring plan, public creditors will form a separate class of their own.
- Class formation may be subject to verification by the court prior to judicial approval of the plan. Once verified by the court, creditors cannot then challenge the plan on the basis of incorrect class formation.
- Voting majority within a class (irrespective of the content of the plan): two-thirds (2/3) majority of the total class debt.
  - Reinforced three-fourths (3/4) majority for classes of secured credits.
  - Syndicate cram-down: if a two-thirds (2/3) or a three-fourths (3/4) majority (as applicable) is achieved within the syndicated debt, the entirety of the syndicated debt is counted as voting in favour of the plan. If the appropriate majority is not reached, individual votes will be counted unless the syndicated debt forms a separate class on its own.
- Cross-class cram-down is possible if approved by either:
  - a majority of classes, provided at least one of the classes voting in favour is either a secured or generally privileged class; or
  - at least one class that is "in-the-money" pursuant to an expert's valuation of the business as a going concern.

- Secured creditors can enforce their claim (i) if there were fewer favourable votes than dissenting votes within their class and (ii) if they voted against the plan. However, the plan can replace the right for payment in cash of the secured portion of the claim (depending on the security valuation) within the following 120 days.
  - If the enforcement proceeds exceed the secured part of the claim, the creditor will keep an amount for up to the rest of the claim (the unsecured part of the claim would be reduced accordingly).
  - If the enforcement proceeds are less than the secured part of the claim, the non-recovered secured part would be lost (the unsecured part of the claim would remain).

CRAM-UP OF SHAREHOLDERS

- A decision at the general shareholders' meeting is not needed for corporate actions included in the plan (debt-for-equity swap, sale of essential assets, hive-down, demerger, etc.) if the borrower is under "actual" or "imminent" insolvency.
- Corporate decisions on implementing the plan are made through a simplified, shorter procedure. Reinforced quorum and majorities do not apply (i.e. ordinary quorum and majorities do apply).

THE RESTRUCTURING EXPERT – A NEW PLAYER

- Required for, among other things, cross-class cram-down restructuring plans, and to advise the judge on safeguarding creditors' rights in connection with the stay of enforcements.
- Appointed by the judge upon request by the borrower or creditors representing >50% of the affected debt (the creditors requesting an expert would assume the expert's fees). Creditors representing at least 35% of the affected debt may also request the appointment of the expert at a later stage in specific circumstances.
- The judge may appoint a different restructuring expert than the one proposed by the borrower/creditors.
- Duties:
  - Assisting the debtor and the creditors.
  - Preparing all required reports and valuations (e.g. best-interest test, cross-class cram-down).
- The expert must be diligent, independent and impartial.
- The debtor remains in full control, but the expert, as a third party, can act as a mediator between the debtor and the creditors.

JUDICIAL APPROVAL (*HOMOLOGACIÓN*)

- Judicial approval of the plan is necessary to:
  - be entitled to claw-back protection for new money, interim financing or any transaction under the plan;
  - cram-down creditors or classes of creditors;
  - cram-up shareholders; or
  - terminate existing contracts in the interest of the restructuring.
- The party requesting judicial approval of the plan can ask that any opposition from other parties be filed and analysed prior to the judicial approval to prevent any subsequent appeal.
- Grounds for dissenting creditors to challenge approval, regardless of whether or not they belong to a dissenting class (if any):
  - Borrower is not in an actual, imminent or likely insolvency situation.
  - Class formation or approval of the restructuring plan not made as per the legal requirements.
  - Plan does not provide for any reasonable prospect of avoiding insolvency and making the business viable in the short and medium term.
  - Plan is more detrimental to creditors than necessary. If the creditor purchased the claim then the detrimental effect on that specific claim would be analysed taking into account the acquisition price.
  - Plan does not satisfy the creditors' best-interest test.
  - Borrower is not up to date with its tax and social security obligations.
- Additional grounds for dissenting creditors belonging to a dissenting class to challenge approval:
  - Non *pari passu* treatment among classes, or a particular class under the plan will be granted shares, rights or assets worth more than the claims.
  - Absolute-priority rule. Restructuring plans that do not comply with the absolute-priority rule may also be acceptable if the judge considers that the plan is "essential to ensure business viability and that affected creditors would not be unjustifiably prejudiced".
  - The debtor not complying with tax and social security obligations if the plan affects public creditors.
- Court of appeal will analyse and rule on the challenge. The decision will be final and not subject to appeal.

- If the court rules in favour of the party challenging the plan, the effects of the plan will not extend to the challenging party but they will be applied to the rest of the affected creditors (except in the event of a lack of majority or incorrect class formation).

NEW TOOLS FOR RESTRUCTURING COMPANY GROUPS

- Third-party release of security interests and guarantees granted by other group members who are not a party to the plan in order to avoid the insolvency of both the borrower and the guarantor.
- Extension of international jurisdiction for restructuring group affiliates with a COMI outside of Spain provided specific requirements are met:
  - Parent company has filed for a stay or judicial approval of a restructuring plan before Spanish courts.
  - The stay and restructuring plan of the affiliate should be confidential (i.e. not registered in the Spanish Insolvency Registry) and therefore not fall within the scope of the European Insolvency Regulation, but may be recognised under other international private law instruments.
  - Efficacy test: necessary to protect restructuring negotiations or the plan's approval and compliance.
  - Jurisdiction exclusively over joint creditors of both the parent and the affiliate.
- The same restructuring expert may be appointed for all group companies involved in the restructuring.
- The group's stay and restructuring plan will be decided by the same judge.

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