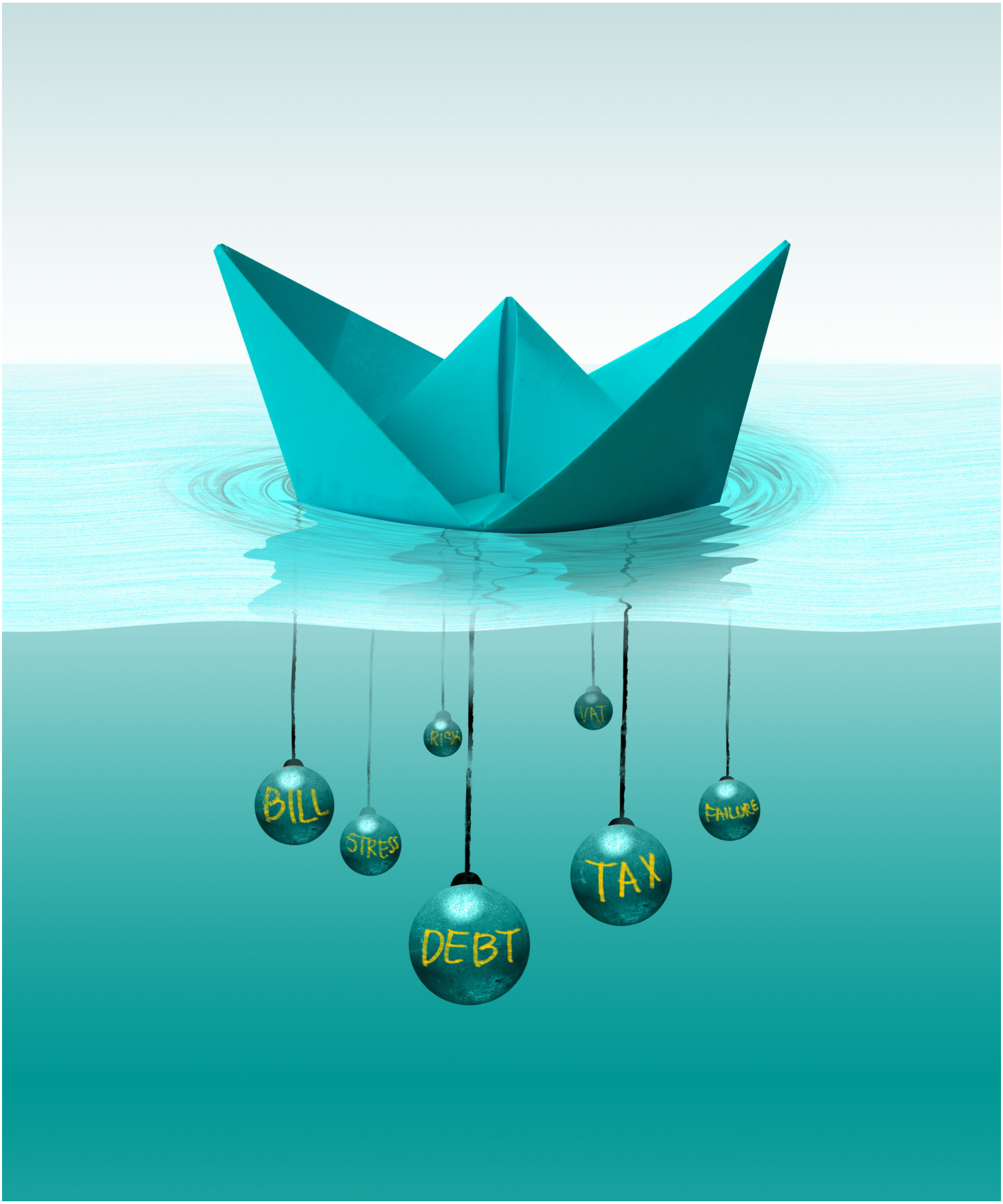
GARRIGUES

RESTRUCTURING AND INSOLVENCY

JUNIO 2016




LAW
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1941-2016 GARRIGUES

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01 SELECTED COURT CASES AND MAJOR SETTLEMENTS

1.1. «Delforca» case: Decision by Barcelona provincial appellate court, February 11, 2016, and judgments by the same chamber, April 19, 2016

A creditor filed a complaint to contest the list of creditors, seeking the recognition of a contingent claim (for being the subject of litigation), because the existence and quantum of the claim were being disputed in an arbitration proceeding initiated before the insolvency order on the debtor which had been stayed by the insolvency judge. The complaint was dismissed at first instance on the argument that, because it was considered that the arbitration had not started, the claim was not the subject of litigation nor therefore could it be considered contingent. The creditor lodged an appeal with a further petition for the commercial court judge to order a stay on any steps potentially affected by the outcome, until the appeal was settled (and among those steps, the holding of the creditor's meeting) and on the payment of subordinated claims (pursuant to article 197.6 of the Spanish Insolvency Law (*Ley Concursal* or "LC")).

The Commercial Court denied in full the appellant's petition for a stay. After the matter reappeared before the provincial appellate court, however, the appellate court ordered postponement of the creditors' meeting until the appeal had been settled. It held in particular that because the proposal for an arrangement provided for the immediate payment of all unsecured and subordinate claims, a detriment could arise to the appellant's rights, as the holder of an unsecured contingent claim, if the meeting were held, and the arrangement were approved and implemented.

The provincial appellate court fully upheld the lodged appeal. In doing so, it reasoned that the arbitration proceeding was "being conducted" when the insolvency order took place, and therefore the claim at issue is the subject of litigation, and consequently, must be included on the list of creditors as a contingent claim.

Elsewhere, in the same insolvency proceeding the insolvent debtor sought (i) termination for breach concerning the "legal relationship" existing between the insolvency debtor and the institution to which the Arbitration Court conducting the proceeding is attached, together with (ii) termination of the arbitration clause that gave rise to the commencement of the arbitration proceeding between the parties. At first instance, the commercial court judge upheld the complaint in full and terminated the "legal relationship" and the arbitration agreement for breach and in the interests of the insolvency proceeding. The provincial appellate court, however, upheld the creditor's appeal in full and dismissed the insolvent debtor's complaint. The first reason being that the lower court's judgment was inconsistent in that the plaintiff only petitioned for termination for breach, and therefore it could not uphold termination in the interests of the insolvency proceeding. Additionally, among other aspects, the appellate court concluded that none of the relationships sought to be terminated contained reciprocal obligations outstanding and having financial content and therefore, they could not be terminated pursuant to article 62 LC.

1.2. Court validation of the refinancing agreement for «Aliwin»: Decsion by Madrid Commercial Court No 6, March 15, 2016

The court validated the refinancing agreement for Aliwin Plus S.L. which attained the affirmative vote of 98.53% of the financial claims and included, among other terms, a reshaping of the credit facility by dividing it into two new tranches: A and B, a three-year rescheduling with respect to the final instalment or final maturity date of tranche A together with a three-year rescheduling for each of the due dates, instalments or interim repayments in tranche A, a tranche B with bullet maturity, new remunerative interest rates, windows for the conversion of all or part of tranches A and B into a participating loan and extending the provision of security to all the creditors, regardless of whether they signed or not. The court also ordered the protection of the refinancing agreement against claw-back actions and the binding nature of the terms on the dissenting creditors from the very moment the decision became final, although under an explicit provision, the refinancing agreement took effect on different dates with respect to the debtor and acceding creditors.

1.3. Mandatory insolvency proceeding on «Hotel Santo Domingo»: Judgment by Madrid Commercial Court No 11, March 16, 2016

The judge upheld a petition for a mandatory insolvency proceeding (due to a general cessation of payments), filed by the vehicle company of the mutual fund that had acquired a number of collection rights from the main financial creditor of the company operating the hotel. Although only two creditors were affected by the company's default on its obligations, the decision not to pay the outstanding claims of creditors that turned out to hold the majority of the company's debts caused the court to find a general cessation of payments, and therefore, the event determining technical insolvency. Despite being a mandatory insolvency proceeding, the judge required the mere intervention by the insolvency manager of the debtor's powers due to the complexity associated with management of the business (hotel industry), the continuity of the company and the potential losses caused by a drastic change in the management of the business, with a stipulation, however, that the insolvency manager could request a reversal of this position and return power to the directors of the insolvent company as soon as they considered they had been sufficiently informed of the course of the business.

1.4. Sale of the productive unit of «Laboratorios Pérez Giménez»: Decision by Cordoba Commercial Court No 1, May 20, 2016

The company that had been awarded the productive unit more than two years earlier requested an extension of the period for the final delivery of the unit and the payment of the price, asserting: (i) that it needed more time to be able to include the final price in the deed of purchase; (ii) that it was necessary to attach to the deed of purchase a certificate of the final nature of the provincial appellate court's judgment setting the final price of the transaction and of the court's decision setting out the covenant between the parties; and (iii) that the steps for the financing party to be able to obtain the security had been delayed. The court expressed its reluctance, and even hinted that the awardee might not have the financial capacity to pay the covenanted sum or that it was even seeking a route to get out of its purchase commitment. It nevertheless granted the acquirer of the productive unit a final and unalterable extension for forty-five days, while announcing the commencement of a parallel process in which potentially interested parties could express their interest in acquiring the productive unit in case the awardee was unable to meet the payment.

02 GROUP OF CASES: SALE OF PRODUCTIVE UNIT AND TRANSFER OF UNDERTAKINGS

2.1. Judgment by Barcelona Commercial Court No 10, December 23, 2015

The insolvency judge awarded a productive unit under the method provided by the Supreme Court (Labor Chamber IV) in connection with transfers of undertakings for employment law and social security purposes. It therefore held that any determination by the commercial court judges concerning a transfer of undertakings is merely a pre-trial determination and is not binding on the labor court judges except for the option to exempt the acquirer from any employee and social security debts which may be covered by the Wage Guarantee Fund pursuant to article 33 of the Workers' Statute ("WS"). Additionally, the insolvency judge held that, in the context of an insolvency proceeding, there is only a transfer of undertakings in the terms of article 44 WT (and therefore the acquirer is exempted from the debt covered by the Wage Guarantee Fund pursuant to article 33 WS) but not so in respect of any debts owed by the insolvent company to the Spanish tax agency or the Wage Guarantee Fund because there is no express legal provision.

2.2. Judgments by Catalunya High Court (Labor Chamber), February 19 and February 23 2016.

In the decision approving the liquidation plan, falling under the wording of the Insolvency Law given by Law 38/2011, the insolvency judge authorized the transfer of a productive unit in which the acquirer accepted a number of workers, and it was explicitly provided that the acquirer was not subrogated to the

transferor's debts to its employees. The workers not included in the productive unit were later dismissed by the insolvent company. In this scenario, some of the dismissed workers applied for a decision holding unjustified dismissal and secondary liability for the acquirer, which was upheld by the Labor Court at first instance. At second instance, however, the Labor Chamber held that the only person with the power to delineate the scope of the subrogation in respect of the employees and the limit on the acquirer's liability is the insolvency judge, whose decision is binding on the labor courts. Any other interpretation would give rise to major legal uncertainty. The chamber also held that the award of a productive with workers in the context of an insolvency proceeding is a court-authorized transfer of assets and not a transfer of undertakings, for which reason neither article 44 WS nor article 149.2 LC would be applicable, so the acquirer would not be answerable for the amounts owed to workers not included in the productive unit.

2.3. *Judgment by the Supreme Court (Labor Chamber), April 13, 2016*

The Supreme Court (Labor Chamber) considered correct the insolvency judge's decision to uphold the collective termination of employment contracts, including those of employees who had filed dismissal claims before the insolvency proceeding, which it supported with the following reasoning: (i) a termination at the will of the employee due to failure to pay salaries or the absence of actual occupation is interrelated with tacit dismissal founded on the same grounds where both arise from the same position of technical insolvency; (ii) the insolvency proceeding inherently attracts (*vis atractiva*) an ancillary proceeding for the collective termination of employment contracts; and (iii) this is precisely why article 64.10 LC provides that any individual termination actions under article 50 WS founded on the economic circumstances or technical insolvency must be stayed after the collective termination procedure within the insolvency proceeding has started. The conclusion being that in the chamber's view, this interpretation of article 64.10 LC must apply by analogy to tacit dismissals founded on the economic circumstances or technical insolvency of the insolvent employer, even if the workers filed the claim before the insolvency order..

2.4. *Decision by Guadalajara Court of First Instance No 4 and Commercial Court, May 11, 2016*

The party acquiring a collection of real estate, facilities and machinery having no associated activity whatsoever or employment contracts in force asked the insolvency judge for a court decision expressly indicating that there was no transfer of undertakings for employment law purposes and therefore no subrogation was required to the outstanding salaries and severance or to the tax and social security obligations before the transfer. The judge granted the petition affirming that the transfer consisted of the sale of a specific asset from the assets available to creditors and not of a productive unit and therefore the transfer could not be considered a transfer of undertakings for employment law purposes.

03 INSOLVENCY ROUND-UP

3.1. *Approval of the Scheme of Arrangement of «Codere»: Order of the High Court of Justice (UK) in the matter of Codere Finance (UK) Limited, October 29 2015*

The High Court of Justice in the United Kingdom approved the scheme of arrangement of Codere Finance (UK) Limited after confirming the following points: (i) the provisions of the Companies Act had been complied with; (ii) the class bound by the arrangement was fairly represented by the creditors who attended the meeting; and (iii) the arrangement "*is such as an intelligent and honest man (…) might reasonably approve*". The fact that the refinanced company had been recently acquired to apply the UK scheme did not preclude its approval, among other reasons, because: (a) the company is subject to English law and has its center of main interests in England; (b) the 18 creditor noteholders holding claims amounting to €250 million (representing 22% of the debt), are domiciled in England; and (c) the expert evidence indicates that the scheme is likely to be effective in other jurisdictions. At all events, the scheme appears to be in the interests of the creditors, in that: (1) it was devised following close consultation with creditors and

has enjoyed an overwhelming level of support from them; (2) no creditor has opposed the scheme; (3) the lack of alternatives available in other jurisdictions; and (4) the judge's declining to sanction the scheme could cause a loss of around €600 million.

3.2. *Claims against the insolvent debtor billed after the insolvency order cannot be attached: Decision by Las Palmas de Gran Canaria Provincial Appellate Court, November 20, 2015*

The insolvency judge held that it was mandatory for all the insolvent debtor's revenues to be included and instructed for the collection rights attached by the Spanish tax agency before the insolvency order to be included in the assets available to creditors. On appeal, the appellate court confirmed that claims billed after the insolvency order cannot be attached irrespective of whether the attachment order is rendered before it, because post-insolvency order claims are also included in the assets available to creditors in the insolvency proceeding, which cannot be encumbered. The chamber stayed the administrative enforced collection proceedings initiated by the Spanish tax agency in relation to outstanding claims billed by it before the insolvency order. In relation to the claims billed after the insolvency order, the chamber held that these cannot be bound by an earlier attachment, and therefore no finding is needed as to their necessity for the company's business.

3.3. *Definition of "integrated enterprise" for insolvency purposes: Judgment by Barcelona Provincial Appellate Court, December 3, 2015*

Barcelona Provincial Appellate Court made a determination on the concept of "integrated enterprise" for insolvency purposes by accepting that the definition includes cases of direct or indirect control, exerted by both legal entities and individuals, among a collection of companies (excluding horizontally integrated enterprises). The chamber held that to find an "integrated enterprise" for insolvency purposes, it is not strictly necessary for there to be a parent "company" and another controlled company among which there is the element of control defined in article 42 of the Spanish Commercial Code; that position of control may be seen in relation to an individual who exerts control with respect to a "controlled" company.

3.4. *Fault-based insolvency: Judgment by Seville Commercial Court No 2, January 5, 2016*

The judgment upholds the existence of willful misconduct or gross negligence in generating or aggravating technical insolvency together with the irebuttable presumption of fault-based insolvency associated with the existence of accounting irregularities. Additionally, the judge ordered payment of the whole of the shortfall, disqualification for 10 years from serving as directors and the forfeiture of any right against the insolvent debtor for every person on the insolvent debtor's board on a joint and several basis, regardless of whether the main decisions were adopted unilaterally by the chief executive, without holding the relevant meetings.

3.5. *Insolvency manager's fee: Judgment by Pamplona Commercial Court No 1, January 18, 2016*

In an ancillary insolvency proceeding, a creditor sought: (i) a reduction of the insolvency manager's fee; (ii) an order for the insolvency manager to deliver payment of the claims owed to the creditor; and (iii) a determination that, in the event of insufficient assets available to creditors, the insolvency manager's fee must fall under article 176bis 5, point 2 LC. The judge only upheld the first petition and placed a limit on the insolvency manager's fee, resulting in the manager only being paid for the common phase, two months of the arrangement phase and six months of the liquidation phase, by considering that the lengthening of that phase had been due to a lack of diligence on the insolvency manager's part.

3.6. *Binding character of the instruction given by interlocutory order to a financial institution: Decision by Valencia Commercial Court No 3, February 5, 2016*

By interlocutory order, the insolvency judge instructed a creditor to unblock the insolvent debtor's bank account. The appellant did nothing to stop the order becoming final, failed to obey the instruction, and instead, requested an amendment of the final documents so as to be granted a preferred right. The petition was denied by the insolvency manager and later, by a court judgment. The appellant later applied for a postponement of the creditors' meeting, which was denied in a further interlocutory order. This new order also instructed the financial institution a second time to unblock the

insolvent debtor's account. The appellant asserted that the order containing the first instruction to unblock the bank account did not meet the *res judicata* test, nor did it prejudge the facts at issue and it considered that the time limit had not precluded its right to contest the classification of its claim according to the final wording. The court held that those arguments did not preclude the binding force of the first interlocutory order and therefore instructed it to "unblock" the account of the insolvent debtor, and consequently, dismissed the appeal, with an official notice that it would be liable for a criminal offense of disobedience if it failed to unblock the account immediately.

3.7. Request for a ruling on unconstitutionality: Decision by the Constitutional Court, February 16, 2016

The Constitutional Court failed to admit a request for a ruling on unconstitutionality as to whether the limited participation of creditors in the assessment section of the insolvency proceeding (together with the rule providing that the insolvency proceeding must directly be held 'accidental' where the insolvency manager and the public prosecutor's office share the same view, regardless of the assertions of any creditor who has appeared in the proceeding) may be contrary to the right to an effective remedy. The court held that this issue had already been clarified by the Supreme Court by ruling that the participation of creditors in the assessment section did authorize them individually to submit arguments for a fault-based assessment. The conclusion being that the conferral of the right to assess the insolvency exclusively on the insolvency manager and on the public prosecutor's office is not arbitrary or disproportionate, nor therefore is it unconstitutional.

3.8. Clawback and revocatory action: Judgment by Murcia Commercial Court No 2, March 18, 2016

The insolvency manager requested partial clawback of a deed and the defendants objected, arguing that the rights to both clawback and revocatory action had expired, because the date of the deed was earlier than two years from the insolvency order, and, than four years from the filing of the complaint. The court concurred that the right had expired, in that, for the clawback action, the two-year time limit starts on the date of the insolvency order not on the petition date. And for the revocatory action, the judge held that the four-year time limit starts on the execution date of the deed because this is when the facts became available to the creditors.

3.9. Conclusion of the insolvency proceeding due to insufficient assets available to creditors: Decision by Valencia Commercial Court No 2, April 1, 2016

The judge ordered the conclusion of the insolvency proceeding because there were no assets, and consequently, the termination of the legal personality of the insolvent debtor and the closure of its page on the relevant public registries. In addition, the judge held that the publicity of the judgment and its publication at the registries must be provided at no cost on account of there being insufficient assets available to creditors. The debtor was nevertheless held liable for payment of all the other claims.

3.10. The elements to be examined in the assessment section: Judgment by the Supreme Court (Chamber One), April 1, 2016

The Supreme Court reasoned that both the insolvency manager's report and the public prosecutor's opinion must express clearly both the petition (*petitum*) and the ground for petitioning (*causa petendi*), formed by the facts and legal grounds supporting the existence of the grounds for assessing the insolvency as fault-based and the resulting determinations. Any alteration to the ground for petitioning that is supported by other facts or considerations, with different consequences, implies an infringement of article 456 of the Civil Procedure Law and of the principle that no new evidence can be admitted in an appeal (*apellatione pendente nihil innovetur*).

3.11. Sale of real estate: Decision by Bilbao Commercial Court No 2, April 5, 2016

Pursuant to article 155.5 LC, the price obtained from realizing the property must be used for payment of the

specially preferred claim, and no sums that the creditor is not required to pay may be deducted from it. Under article 106 of the Law on Local Finances, it is the vendor/insolvent debtor who must pay the tax on the increase in urban land value. Therefore this tax cannot be deducted from the sale price. No rule authorizes the insolvency manager to charge to the mortgage creditor any amount of tax for which it is not liable.

3.12. Defining elements of de facto directors: Judgment by the Supreme Court, April 8, 2016

The Supreme Court specified the characteristic elements of the de facto director, namely: (i) they must carry on a management activity associated with a corporate director; (ii) this activity must be carried out systematically and on a continued basis with a qualitative and quantitative intensity; (iii) it must be performed separately, with independent decision-making power and with the company's support; and (iv) the *de facto* director must not be officially appointed. After determining the definition, the chamber held that the supervision and monitoring activities on public funds that were carried out by a government-controlled company (Sociedad Estatal de Participaciones Industriales), at an entity in the public group to clean up its accounts before privatizing it are not to be confused with the tasks related to managing or running the insolvent debtor, and therefore, held that if there is no *de facto* director the appellant's claims cannot be classified as subordinated claims.

3.13. Netting of claims in the arrangement compliance phase: Judgement by the Supreme Court (Chamber One), April 8, 2016

In the arrangement compliance phase, the insolvent debtor brought action to claim debts against a third party, which objected by asserting that the debts had been netted, and arguing that the sums it owed to the insolvent debtor had to be netted against the sums owed to it by the insolvent debtor under the debt recomposition terms stipulated in the arrangement. The chamber held that, until there had been a finding of compliance or breach of the arrangement, it could only allow the netting of the amended sums (under the debt recomposition provision stipulated in the arrangement) which had actually fallen due according to the terms of the arrangement itself. The chamber also held that the jurisdiction to decide on both the action brought and on the netting lay with the Court of First Instance.

3.14. Recommencement of the assessment section due to breach of the arrangement: Judgment by the Supreme Court (Chamber One), April 13, 2016

The Supreme Court reaffirmed its view concerning the grounds that must be sought to recommence the assessment section of the insolvency proceeding following a breach of the arrangement, stating that an assessment section recommenced following a breach of the arrangement may only deal with points that could not be examined in the first assessment section that was commenced, which means that the decision on the grounds for assessment in insolvency proceedings in which a "tough" arrangement was approved (which in turn gave rise to a first assessment section) must be confined to whether the inability to comply with the arrangement is attributable to the insolvent debtor. In the case examined, the only reason for breach of the arrangement was that it was not feasible from the outset, and this reason could not be attributed to the persons named as being associated with the assessment, who even objected to its approval.

3.15. Request for a preliminary ruling: Judgment of the European Court (Third Chamber), April 21, 2016

The court ruled on the ability of the insolvency judge to analyze the unfairness of terms on which the claims in an insolvency proceeding are based and order the related consequences regarding their recognition. The court held that Directive 93/13/EEC precluded any national legislation which: (i) does not allow the insolvency judge to examine of its own motion any unfairness of contractual terms on which the claims in insolvency proceedings are based; (ii) only allows the judge to perform this examination in relation to unsecured claims; and (iii) restricts the judge's examination to a restricted number of complaints based on whether they are time-barred or have been paid. Moreover, article 10.2 of Directive 2008/48/EC requires the national court hearing a dispute to examine of its own motion whether the obligation to provide information laid down in that provision has been complied with and to establish the

consequences under national law of an infringement of that obligation. Accordingly, the Court affirmed that the national courts have the jurisdiction to establish all the consequences of a finding that certain terms are unfair to ensure that the consumer is not bound by them.

3.16. Realization of assets subject to a specially preferred right in the liquidation phase: Decision by Madrid Commercial Court No 1, April 29, 2016

In the context of a realization of property subject to a specially preferred right in the liquidation phase, the insolvency judge held that the purpose of paragraph two of article 155.4 LC is to avoid the system of security interests being 'blasted to pieces' in insolvency proceedings, and to this end, grants a veto right to the financial creditors in any realization of proper ty at its real market price below the appraised price. On the basis of this interpretation, the judge approved all the objections and amendments requested by the financial institutions to the liquidation plan filed by the insolvency manager.

3.17. Assessment as accidental insolvency: Judgment by Barcelona Provincial Appellate Court, April 29, 2016

The appellate court upheld a number of appeals against the judgment by the insolvency judge assessing the insolvency as fault-based and revoked the lower court's judgment, to hold that the insolvency was non-fault-based. According to the chamber, the insolvency must not be held fault-based as a result of the delay in petitioning for it, where it is evidenced either that the debtor cannot be blamed for the delay, or that the delay did not aggravate the company's insolvency. In the examined case, even though it had been evidenced that the airline company under an insolvency proceeding was technically insolvent seven months before the petition for an insolvency order, the directors' actions were geared towards securing the continuity of the enterprise. It was only when it became apparent that the company would not be able to continue operating that they petitioned for an insolvency order.

04 GARRIGUES ARCHIVES

4.1. Meetings and events

The 2016 TMA Europe conference to be held in Rome entitled "Increasing performance through turnaround culture and values" is a must for all turnaround practitioners investors and other professionals that are involved in distressed environments.
The speakers and participants will discuss the economic business environment in Europe, focusing on lucrative areas of potential investment for the entire global investment community. There will also be several panels debating a range of turnaround topics, insolvency and turnaround legislation in various European countries from North to South. In addition to some real life examples, NPLs will also be discussed and issues affecting the whole of Europe will be debated.
Garrigues partners will sit on two panels of specialists: "*Equity cram-down and EU Harmonization*" (Adrián Thery) and "*Latest trends, techniques and tools for SME Debt Restructuring in the main Continental European jurisdictions*" (Juan Verdugo)

4.2. Publications

• «**Something new under the sun: trends in Spanish non-performing loan (NPL) trading**» [Berdullas Pomares, González Pila and Álvarez Úcar], Butterworhs Journal of International Banking and Financial Law, May 2016.

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